PACIFIC MUTUAL LIFE INS. CO. REHABILITATION CASE

Supreme Court of the United States

October Term, 1938. No. 21.

WILLIAM H. NEBLETT, Et Al., - - - *Petitioners,*

versus

SAMUEL L. CARPENTER, JR., Insurance Commissioner of the State of California.

On Writ of Certiorari to the Supreme Court of the State of California.

BRIEF FOR THE INSURANCE COMMISSIONER OF CALIFORNIA.

1. California did not violate the "contract" clause, when—in rehabilitating the business of an insolvent insurance company—she devoted *all* assets exclusively to the payment of *all* creditors; even though she gave one class of policies a different treatment from all other policies.

That difference was absolutely necessary (1) to preserve the "going concern" business so as to continue 100% insurance protection to 250,000 policyholders who needed it, (2) to save millions of dollars of assets which would otherwise have been lost, and (3) to avoid a forced-sale liquidation with the inevitable delay, expense and losses—all with the result that the alleged 50,000 subordinated policies will now (a) receive more than on liquidation and (b) probably receive, in turn, 100% re-insurance.

2. Petitioners elected not to bring up any of the evidence on the seven weeks' hearing. In its absence, it must be presumed that such evidence (if here) would support the judgment and show (1) that there was no ultimate or substantial difference in treatment and (2) that the reduction in benefits [limited to "Non-Can" Active Lives] was temporary and beneficial to those affected.

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LIST OF AUTHORITIES.

Statutes.

[References Required by Rules 12 and 27.]

Opinion Below: *Carpenter v. Pacific Mut. Life Ins. Co.*, 10 Cal. (2d) 307; R. 1509-1544.

Jurisdictional Authority: Judicial Code §237(b), as amended by Act of February 13, 1925 (Ch. 229, 43 Stat. 936).

Statutes Involved: California Ins. Code (1935), Ch. 145, Part 2, Ch. 1, Art. 14 §§1010-1061; United States Constitution, Art. I, Sec. 10; 14th Amendment, Sec. 1.

Date of Judgment, Etc.: Dec. 4, 1936 (R. 1378-1395).

Nature of the Case, Rulings, Etc.: On July 22, 1936, Pacific Mutual Life Insurance Co. was insolvent. The Insurance Commissioner of California summarily seized its assets and business, and proceeded to operate them (through the formation of a New Company) pending a statutory Rehabilitation—the seizure being confirmed, and the operation authorized by the Co rt.

On December 4, 1936, after seven weeks' continuous trial, the Court (Willis, J.) sustained the proposed Rehabilitation, and authorized the execution of, and full performance under, a certain *revised* "Rehabilitation and Reinsurance Agreement" [called "Rehabilitation Plan"] (R. 1396-1444).

On December 7, 1937, the Supreme Court of California *affirmed* that judgment; and held that there was no violation of (*a*) California's Constitution or laws, or (*b*) the Federal Constitution's "due process," "equal protection," or "contract" clauses (R. 1509).

On May 16, 1938, *certiorari* was granted (304 U. S. ; R. 1546).

IN THE

Supreme Court of the United States

October Term, 1938. No. 21.

WILLIAM H. NEBLETT, ET AL., - - - - - *Petitioners,*

v.

SAMUEL L. CARPENTER, JR., INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA.

On Writ of Certiorari to the Supreme Court of the State of California.

BRIEF FOR THE INSURANCE COMMISSIONER OF CALIFORNIA.

The sole question involved is whether California had the power [consistently with the Federal Constitution] to rehabilitate a local *insolvent* insurance company's business, *first,* by organizing a New Company, and then, *second,* by executing with the New Company a certain "Rehabilitation and Reinsurance Agreement";* which Rehabilitation Plan treated *some* of the so-called "Non-Can" policies [*i. e.,* Non-Can policies on **Active**† Lives] *differently* from all the rest of the policies—all of which (1) was done pursuant to specific authority given by the California Insurance Code, and (2) has been sustained by the

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*For brevity, hereafter sometimes called "Rehabilitation Plan."

†For definition of "Active" and "Disabled" Lives, see p. 16, note, *infra.*

California Courts (*Carpenter* v. *Pacific Mutual Life Ins. Co.*, 10 Cal. (2d) 307; R. 1509—which, for brevity will be often cited as OPINION R. —).

The petitioners [four‡ dissatisfied policyholders of the insolvent Company] insist (1) that the Rehabilitation Plan [for preserving its profitable business as a "going concern" and gradually applying all its assets, *tangible and intangible,* to the discharge of its obligations] is discriminatory, denies "due process," and impairs their policy contracts; and (2) that its assets should be liquidated by a quick sale to the highest and best bidder; and the cash proceeds thereof applied to the *pro rata* payment of all its creditors, including future, unaccrued, and unliquidated policy obligations (R. 990, 1233, 1347-1349).

CALIFORNIA'S LAW FOR REHABILITATION OF INSOLVENT INSURANCE COMPANIES.

In 1935, California adopted an Insurance Code, with a special chapter on "Proceedings in cases of Insolvency and Delinquency" of insurance companies, the Rehabilitation sections of which were "copied substantially from similar provisions in the New York Insurance Law" (R. 1532; Cf. N. Y. Ins. Law Art. XI, §400 *et seq.;* Cal. Ins. Code §1010 *et seq.,* §1043). The constitutionality of that New York Law has been repeatedly sustained [or assumed to be valid] in many State and Federal decisions cited in the margin.*

‡Out of about 275,000 policyholders.

**Van Schaick* v. *Title & Mtge. Guarantee Co.*, 264 N. Y. 69; *Application of People by Van Schaick,* 239 App. Div. 490; affirmed 264 N. Y. 473; *In re New York Title & Mtge.*

Numerous States, California, New Jersey, New York, etc., have adopted statutes, reflecting the spirit of the *Blaisdell* case, 290 U. S. 398; *Doty* v. *Love,* 295 U. S. 64, and the new Frazier-Lemke Act,[1] to provide for the rehabilitation [sometimes called "reorganization"] of insolvent or financially distressed insurance companies, which are denied both the benefits of the Bankruptcy Act[2] and of an ordinary Federal equity receivership.[3]

The purpose of these State "rehabilitation" statutes was:

First: To prevent corporate assets from being torn to pieces at the suit of rival creditors, resulting in dismemberment with great waste and inequality; and to avoid the sacrifice of assets and their unequal distribution by writs of execution as between local and foreign policy holders (*Clark* v. *Williard,* 292 U. S. 112, 123, 127-129; s. c. 294 U. S. 211, 214-215).

Second: By progressive liberalization in the administration of insolvent insurance corporations [having vast numbers of policyholder-creditors] "to pre-

Co., 156 Misc. 186; *In re Bond & Mtge. Guarantee Co.*, 157 Misc. 240; *In re Casualty Co. of Amer.*, 244 N. Y. 443; *State* v. *Price,* 129 Neb. 433; *Natl. Surety Corp.* v. *Nantz,* 262 Ky. 413; *Thrower* v. *Kistler,* 14 F. Supp. 217; *Natl. Surety Corp.* v. *Ellison,* 88 F. (2d) 399 (C. C. A. 8th); *Jacoby* v. *Bond & Mtge. Guarantee Co.,* 72 F. (2d) 420 (C. C. A. 2d).

[1] *Wright* v. *Vinton,* 300 U. S. 440, 456, 470; *Adair* v. *Bank of American Assn.,* 303 U. S. 350.

[2] U. S. C. A. Title 11 §§22, 207; Act June 25, 1910, 36 Stat. 839; Glenn on Liquidation §265; *Union Guarantee & Mtge. Co.* v. *Van Schaick,* 75 F. (2d) 984.

[3] *Pennsylvania* v. *Williams,* 294 U. S. 176.

vent a sacrifice of the creditor's interest"; "to avert the evils of liquidation"; to provide "opportunities for the rehabilitation" and "the maintenance [of the business] as a going concern" through "the continuance of the operations" (*Louisville Bank* v. *Radford,* 295 U. S. 555, 597; *Adair* v. *Bank of America,* 303 U. S. 350; *Wright* v. *Vinton Branch,* 300 U. S. 440; *Wright* v. *Union Central Life,* 304 U. S.   ).

Third: To provide a comprehensive method (under judicial control after full notice and hearing) to ensure the best results for the policyholder-creditors *as a whole,* (i) **by enabling them to keep their insurance in force, instead of a compulsory lapse when they might have become uninsurable,** and (ii) by realizing, at full value, the tangible assets, and by utilizing the Company's agency force and good will, instead of accepting "forced sale" prices for tangible assets alone—even if in the course of such a rehabilitation of the business of the *insolvent company*—(iii) some minor readjustments become necessary in the strict legal rights of the policyholders-creditors—all on the theory that the insurance business [with its many millions of policyholders and beneficiaries as common creditors] is sufficiently affected with a public use (*German Alliance Ins. Co.* v. *Kansas,* 233 U. S. 389) to justify protective rehabilitation proceedings ("Life Insurance Reorganization," 29 Ill. L. Rev. 559, 575).

Relevant Statutes.

[Insurance Code of California (1935), Ch. 145; Part 2, Ch. 1, Art. 14, §§1010-1061. *Cf.* Stat. (1935), pp. 540-553.]

§1043. In any proceeding under this article, the commissioner, as conservator or as liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary mutualize or re-insure the business of such person, **or enter into rehabilitation agreements.** Such rehabilitation or reinsurance agreements shall provide that, subsequent to the date thereof, and for such period of time as the commissioner may determine, no investment or reinvestment of the assets of the person rehabilitated or reinsured shall be made without first obtaining the written approval of the commissioner.

[All the relevant statutes are in the Appendix, p. 95, *infra*.]

STATEMENT OF FACTS.

I. *Pacific Mutual's business* (*1868-1936*). On December 31, 1935, "The Pacific Mutual Life Insurance Company *of California*," hereafter generally called "Old Company" (with $215,000,000 assets) was engaged in two kinds of insurance in over *forty* States, *i. e.*:

A. *Life Insurance.* It had 200,000 policyholders insured for $600,000,000 life insurance. The legal Reserve therefor was over $170,000,000. That part of the business was sound with a Surplus of over $5,000,000* (R. 5-6, 24, 30, 31, 846; Opinion R. 1518-9, 1528, 1534-5, 1540).

*Nearly $6,000,000 by July 22, 1936.

B. *Accident and Health Insurance.* In addition, it had outstanding about 75,000 policies of Accident and Health insurance, of which about 50,000 were non-cancellable "Disability" policies (referred to in this Record as "Non-Can" policies) *containing no life insurance and no loan or surrender values;* under which (in addition to certain "accident" benefits), if a policyholder became *disabled,* Pacific Mutual *agreed to pay a monthly income* to the disabled policy-holder—on account of which, in July 1936, there was (*a*) a $20,000,000 liability on account of already **Disabled** lives (R. 29, p. 16, *infra*), and, in addition (*b*) a further $25,000,000 liability to take care of the future disablement of then **Active** lives;—to meet which $45,000,000 liabilities, Pacific Mutual had only $20,000,000 Reserve (R. 29-30).*

This "Non-Can" business suffered large disability losses, getting worse every year, until the Company, as a whole, became insolvent (R. 3, 31, 40, 324, 847-8, 1385-6, 1535).

II. *Insurance Departments of Six States reported Pacific Mutual to be insolvent.* On July 21, 1936 (af-

*Pacific Mutual *became insolvent* solely on account of its *Accident* Department where the "Non-Can" *premiums* were *hopelessly inadequate* to provide for the Disability Benefits (R. 324, 847-8, 1535, 1540). This resulted on December 31, 1935, in the Accident Department piling up a $20,000,000 *present* liability for future payments to "Non-Can" policyholders *already* disabled, *i. e.*, Disabled Life Reserve; and a then *present* liability of $25,000,000 for future payments to "Non-Can" policyholders *not then disabled, i. e.*, Active Life Reserve—an aggregate amount of $45,000,000 which was far beyond the capacity of the Pacific Mutual (even as a whole) then to provide (R. 29-31)—**Result: Insolvency.**

ter 4 or 5 months' investigation) the Insurance Departments of six States made a joint Report that as of December 31, 1935, Pacific Mutual's *liabilities* were nearly ***Eighteen Million Dollars*** ($18,000,000) *more* than its *assets;* that the Accident and Health business (largely composed of "Non-Cans") showed a *deficit of over Twenty-three Million Dollars* ($23,000,000); and that

> "immediate action must be taken to protect policyholders" (R. 30-32).

III. *California's "immediate action to protect policyholders" by a statutory Rehabilitation of Pacific Mutual.* On July 22, 1936, Carpenter (as Insurance Commissioner) took the following statutory—and practically simultaneous—steps to protect the policyholders:

1. He made the statutory finding that Pacific Mutual is "insolvent" and "in such condition that its further transaction of business will be hazardous to its policyholders, its creditors, and to the public"; and he then took summary possession of all its assets and business—as Ins. Code §1013 specifically authorized him to do *without* the necessity of any court order (R. 35, 324, 997-1001; OPINION R. 1527-9, 1533).

2. He petitioned the State Court [Los Angeles] to appoint him statutory Conservator and Liquidator of Pacific Mutual, with power (*a*) to take over and operate all its assets and business, (*b*) to work out a Plan of Rehabilitation, and (*c*) to execute a proposed

Rehabilitation Agreement, copies of which previously prepared Plan and Agreement were filed therewith (R. 1-102). Jurisdiction attached and Pacific Mutual appeared and consented (Ins. Code, §§1011-1015; R. 33, 48).

3. He organized a new "Pacific Mutual Life Insurance Company" (hereafter called New Company), purchasing its entire $1,000,000 Capital Stock with $3,000,000 of Old Company's cash (thereby giving to New Company $1,000,000 Capital Stock and $2,000,000 Surplus).

He executed the Rehabilitation Agreement* with New Company (R. 152-182); and he transferred to New Company all of Old Company's assets, except the Capital Stock of New Company, and any claims arising on account of any wrongful acts of any of the officers, etc., of Old Company (R. 183-190, 193, 850, 1387, 1397).†

*It was slightly amended and re-executed the next day, July 23 (R. 108-9; 142-3; 193-225). It is somewhat different from the *revised* Plan (finally approved on December 4, 1936, and executed) which is the subject of this *certiorari*.

†Pacific Mutual's financial difficulties had become more or less widely known in California and in other States, even prior to the publication of the Report (R. 4, 235); and as the March-July investigation progressed, the Insurance Commissioners of the six States became fully aware of the Company's insolvent condition (Glenn on Liquidation, §25, p. 48).

The California Insurance Commissioner had been conferring for some days with his official legal adviser, the Attorney General of California, and also with some of the Company's officers (not believed to be responsible for certain questionable acts, R. 31, 938, 968, 970-980), in order that, simultaneously with the imminent publication of the Joint Report, he could summarily seize all Pacific Mutual's assets, and effect a Rehabilitation, so as (*a*) to preserve the Company's valuable business as a "going concern," and (*b*) to avoid the loss inevitable upon disintegration where its 275,000 policyholders and creditors would be engaged in a race to get the most possible out of the wreckage (R. 234, 579-581, 1540).

4. He had obtained Court orders (by the voluntary appearance and consent of Old Company) authorizing his proposed acts (R. 33-4, 48-9, 142, 226); but his actions acquired no additional validity by the *orders,* as they were void because of the subsequently ascertained disqualification of EDMONDS, J., who happened to sign the early orders in this case (R. 323; OPINION R. 1526-7).

5. New Company ["as a corporate agent to assist" the Insurance Commissioner, R. 851, 1528, 1537-8] at once began functioning with the assets and business of Old Company, (*a*) by carrying on the old business to the extent that it had assumed Old Company's obligations, and (*b*) by continuing to write new business with the Old Company's office and agency organization (R. 850-1; OPINION R. 1528-9).

IV. ***Objections to the proposed Rehabilitation; and the discovery that Edmonds, J., was disqualified.*** Very promptly (August 6-11), Mr. Neblett and many policyholders, stockholders and directors of Old Company filed Intervening Petitions attacking the Rehabilitation proceedings for various reasons (*i. e.,* fraud, false representations, conspiracy, preferences, incapacity and malfeasance of the old management for past ten years, etc.); and as in violation of (*a*) the California law, and (*b*) the "due process", "equal protection" and "contract" clauses of the Federal Constitution (R. 233-321).

On August 11 it unexpectedly developed that EDMONDS, J. had a $5,000 policy in Old Company (R. 323);

and consequently his five orders of July 22-23 (R. 34, 49, 103, 142, 226) were *ipso facto* void (OPINION R. 1526-7).

V. *Carpenter re-appointed as Conservator; his prior appointment ratified; directed to operate the business and to submit a Plan of Rehabilitation.* On August 11, the Court (WILLIS, J.), considered anew the Commissioner's application to be appointed Conservator and Old Company's consent thereto, both filed July 22, 1936; and the Court found [and entered an order that Insurance Commissioner had found R. 324] that Old Company is "insolvent" and "is in such condition that its further transaction of business will be hazardous to its policyholders, its creditors and to the public." To safeguard the situation, the Court (WILLIS, J.), also *ratified* the order of July 22 appointing Carpenter as Conservator; then *re-appointed* him as Conservator; vested in him the fee simple title to all Old Company's assets; directed him to operate Old Company's "business and affairs . . . as a going insurance business"; and to prepare a rehabilitation plan to be submitted to the Court (R. 1, 33, 322-328, 997-1001; OPINION R. 1521-2, 1529).

On August 17 the Court (WILLIS, J.) directed the Conservator and New Company to continue to perform under the earlier plan of rehabilitation of July 22-23 (R. 351, 1395, OPINION R. 1528-9).

VI. *Why California adopted Rehabilitation instead of a sale in Liquidation.* Upon the Commissioner's "finding" that Pacific Mutual was insolvent, his

summary seizure of its assets, and his application to the State Court (p. 7, *supra*, R. 3, 324-5, 997-1001, 1525, 1528-9),—as Bankruptcy and a Federal equity receivership are denied to insurance companies, p. 3, *supra*, —the Commissioner had to decide whether (*a*) to ask for appointment as Liquidator to "liquidate and wind up the business," or (*b*) to enter into a Rehabilitation Agreement (Ins. Code §§1013-1019, 1043; Opinion R. 1533-4.

California (acting through its Insurance Commissioner, and in accordance with its public policy) decided that it was impossible to remove the causes which led to the Pacific Mutual's difficulties; and that, instead of liquidating the company, with the consequent delay, waste, losses, and uncertainty as to the various "measures of damage," applicable to the many different groups of policies, it was preferable [through the organization of a New Company and entering into a Rehabilitation Agreement with it] to reorganize—not Old Company *as a corporation*, but the *business* which Old Company had—and to save it as a "going concern" in order to realize the millions of dollars of asset value in its agency force and in its "going business"; thereby to continue insurance protection for those needing it, particularly those who had become uninsurable; and ultimately to pay 100% on all policy obligations (pp. 18, 20, 21, *infra*; Opinion R. 1528, 1534-5).

For these reasons, in this case, California determined upon Rehabilitation instead of "liquidation." **It is impossible here to consider the wisdom of that course, as the seven weeks' testimony on the subject is not**

included in the Record. The State acted; and the Supreme Court of the State has sustained that action in every particular.

VII. *Revised Rehabilitation Agreement; objections thereto; and Order to Show Cause.* On September 25, 1936 (after extended conferences between the Insurance Commissioner, his legal and actuarial advisers, policyholders, stockholders, general agents and creditors of Old Company, R. 1271-2, 1523-4), the Insurance Commissioner submitted a revised Rehabilitation Plan, and petitioned (*a*) for authority to execute it, and (*b*) for a ratification of his *ad interim* actions in carrying on the business (R. 846-904).

On the same day, the Court entered an "Order to Show Cause" why the Court should not authorize and confirm the revised Rehabilitation Plan and all actions of the Commissioner and New Company theretofore taken (R. 905-913).*

In the meantime, there were filed other proposed plans for liquidation or reorganization [135 printed pages; including the original and revised "Giannini" plan for "liquidation" R. 1172-1188, 1350-1368; Opinion, R. 1524]. About *sixty* Intervening Petitions and Responses to the order to show cause were also filed on behalf of *two hundred* policyholders, stockholders

*Ordering notice to be given parties litigant, Insurance Commissioners of all States where Old Company did business, and to each policyholder and creditor of Old Company, by first class mail, posting and newspaper publications; Order returnable October 19, 1936 (R. 905-913).

On October 8, the Court (Willis, J.) amended, *nunc pro tunc*, the orders of July 22 and August 11, by slightly altering certain recitals, in order that the orders might "recite the facts actually appearing to the court" at the time the orders were entered (R. 997-1001; Opinion R. 1524; Cf. R. 34, 323).

and agents of Old Company, and Insurance Commissioners of various States (720 printed pages)—the Insurance Commissioner of Louisiana, the Old Company's General Agents, and one Policyholders' Committee supporting the Insurance Commissioner's revised Rehabilitation Plan, while all the others attacked the Plan on many grounds—both under the California law, and under the "due process" and "contract" clauses of the Federal Constitution.†

VIII. *Seven weeks' Judicial Hearing on the revised Rehabilitation Agreement and Objections thereto.* For about seven weeks (October 19-December 4), the Court (WILLIS, J.) held continuous hearings for, and against, the Rehabilitation Plan, during which "many persons representing various interests were represented"; "evidence both oral and documentary" was introduced; and "full opportunity afforded to all persons . . . to state, discuss and urge any and all objections they, or any of them, might have to the proposed rehabilitation and reinsurance agreement or to these proceedings", including various plans different from that proposed by the Commissioner* (R. 1378-1383; OPINION R. 1524).

†R. 233-321, 329-464, 475-483, 538-547, 589-765, 773-827, 831-845, 914-989, 1002-1007, 1150-1159, 1192-1210, 1237-1245, 1274-1281, 1288-1297, 1314-1318.

*"One such plan was proposed by L. M. Giannini, who suggested the liquidation of the Old Company through a sale of the assets and business to him. This plan was endorsed by the insurance commissioner of the State of Washington, by two large groups of policyholders, and by various individual policyholders [including Mr. Neblett, R. 1347-1368]. . . . At the hearing full opportunity was given to all who appeared to submit evidence and argue their contentions" (OPINION, R. 1524). These suggested

THE COMMISSIONER'S REHABILITATION PLAN

The Rehabilitation Plan (47 printed pages; R. 1396-1443) contains many detailed and technical provisions unnecessary to be considered here. Its substantial provisions may be briefly summarized as follows:

I. Commissioner organized a New Company; subscribed for its entire $1,000,000 (par value) capital stock; paid for it with $3,000,000 cash out of Old Company's assets, and thereby gave to New Company:

NEW COMPANY'S CAPITAL STRUCTURE	CASH
Capital Stock (fully paid up)	$1,000,000
Surplus (paid in)	2,000,000
Total Capital and Surplus (paid in)	$3,000,000

Commissioner thus retained as "trustee" for the benefit of Old Company's policyholders and creditors (p. 8, *supra;* R. 1404; OPINION R. 1526, 1534, 1539),

(*a*) Entire $1,000,000 capital (par value) stock of New Company (represented by $3,000,000 cash);

(*b*) All assets of Old Company (except the $3,000,000 cash paid to New Company for its entire capital stock); and

(*c*) Old Company's claims on account of any wrongful acts of its officers, directors, etc.

Plans cover about 135 pages (R. 1056-1094, 1172-1191, 1211-1232, 1319-1377).

The Giannini plan (which was favored by most of the opposition) was based on the same legal principles as the Commissioner's plan, to wit, 100% re-insurance of Life policies; and a *graduated scale of reduced percentages* of re-insurance for Non-Can policies —to be restored to 100% only so far as certain funds made restoration possible.

II. Commissioner then transferred to New Company (*b*) *supra*, viz., all of Old Company's remaining assets [except (*a*) and (*c*)], which had a value of over $210,000,000 on December 31, 1935* (R. 1388; 1397-8).

III. New Company agreed to "re-insure and assume" as of July 22, 1936, Old Company's liability under all its policies (including "Non-Can" policies) in force on July 22, 1936, subject to the following provisions (R. 1400, 1412):

A. All Policies of Every Kind (<u>except</u> "Non-Can" Policies):

New Company Agreed

(1) To "re-insure and assume" [100%] Old Company's entire liability on all such policies in force July 22, 1936, including Life, Endowment, Accident and Health Insurance, Annuities, etc. (R. 1400-1402, 1410);

(2) To *"pay in full . . . all policy claims* against the Old Company," whether arising *before or after* July 22, 1936, to-wit: Death losses, Annuities, Disability, Accident and Sickness Benefits, etc., etc. (R. 1402-3);

(3) To establish separate "Participating" and "Non-Participating" Life Departments; and to allocate to them, for their respective separate benefits, that portion of Old Company's assets appearing on its Life Department's books on July 22, 1936† [less $4,792,118.97] in the ratio in which such assets stood credited to the "Participating" and "Non-Partici-

*Increased by normal premium and interest receipts (less disbursements) to about $220,000,000.

†On Dec. 31, 1935 this was.......... $188,000,000 (R. 22)
On July 22, 1936 this was.......... 191,500,000

pating" Departments respectively (R. 1403-4; 1408-9);

(4) To "establish reserves against all policies and policy liabilities of the Old Company subject to assumption or re-insurance hereunder" in accordance with the Commissioner's requirements (R. 1421).

(5) To pay to the Liquidator an amount equal to the Reserves so originally established on July 22, 1936, against the policies of those who became *non-assenting* policyholders (R. 1422).

B. All "Non-Can" Policies:

New Company Agreed

(1) To establish reserves as required by the Commissioner (*a*) for full [100%] benefits on all **Disabled** Lives, and (*b*) for the reduced benefits [20% to 90%] on **Active** Lives (R. 1421, 1413-1415).

(2) **Disabled Lives***; **"To pay all disability benefits under Non-Can Policies** for disabilities commencing *prior*" to July 22, 1936, to-wit: to pay all monthly income benefits which had fallen due *in the*

*The expressions (1) "Active Lives" and "Active Life Reserves," and (2) "Disabled Lives" and "Disabled Life Reserves" refer, respectively, to the policies and to the mathematically calculated Reserve thereon, of those persons holding "Non-Can" policies (1) who have *not* become disabled, *i. e.*, are still *active, healthy* persons, and (2) who have become *disabled*, and who are entitled to receive *monthly* Disability Income Benefits so long as they live and continue disabled.

The reserve per $100 monthly benefit *is much larger* for a *Disabled* Life than for an *Active* Life, because the probability of the Company having to pay future successive monthly benefits *is tremendously greater* in the case of an *already* Disabled person (where the sole contingency is whether he will *live* disabled until the successive payments fall due), than it is in the case of an *Active* Life (healthy person) where *two* contingencies must *both* occur before the Company will have to pay anything, *i. e.*, (i) he must *become disabled*, which is only a possibility, and (ii) even after becoming disabled, he must also live disabled; and (iii) at worst, a comparatively small percentage of healthy persons become disabled.

past or should become due *in the future* on *Disabled* Lives, where their disability commenced *prior* to July 22, 1936;

To pay to the Liquidator an amount equal to the Disabled Life Reserve so originally established under (1) *supra* against the policies of those who became *non-assenting* policyholders (R. 1415, 1421-1422);

(3) **Active Lives**: To "reinsure and assume" as of July 22, 1936, Old Company's liability under Non-Can Policies upon *Active Lives* (*i. e.*, policyholders who were *not* disabled on July 22, 1936); **but only for 20% to 90% of the original monthly Income Benefit provided in Old Company's Non-Can Policies** (R. 1412-1414), to-wit:

POLICIES ISSUED IN	PERCENTAGE ASSUMED
1918–1920	20%
1921–1925	35%
1926–1928	45%
1929–1930	55%
1931	65%
1932–1935	90%

To pay to the Liquidator an amount equal to the Active Life Reserve so originally established under (1) *supra* against the policies of those who became *non-assenting* policyholders [R. 1421-1422].

C. Accident and Health Department:

To establish a separate Department for its Accident and Health Insurance (including Non-Can Policies), and to allocate thereto (R. 1410),

(*a*) $1,792,118.97; and also
(*b*) The (nearly) $27,000,000 assets* credited on Old Company's books to its Accident and Health Department as of July 22, 1936.

IV. From the funds available for its general corporate purposes [including certain earnings aris-

*On Dec. 31, 1935 this was..........$27,000,000 (R. 22)
On July 22, 1936 this was.......... 26,400,000

ing from the Participating, and all earnings arising from the Non-Participating and Accident and Health Departments] New Company shall transfer all such funds (not reasonably required for its proper conduct as a "going concern"), to a "**Special fund**" for the restoration of benefits under Non-Can Policies; the "**Special fund**" to be used for the purpose of paying additional disability benefits on Non-Can Policies in excess of the amounts required to be paid (p. 17, *supra*), to the end that Non-Can Policies may ultimately receive [100%] all benefits, with 3½% interest on the deferred restorations (R. 1416-1419).

V. New Company agreed:

(1) To pay in full Old Company's State and Federal taxes, wages, salaries, pensions, current bills and expenses incurred prior to July 22, 1936 (R. 1419-1420); and

(2) To pay to the Liquidator certain sums [as provided for in the Agreement] towards enabling the Liquidator to pay *non-assenting* policyholders' claims, in the amounts finally allowed against the Liquidator (R. 1422-1427).

VI. Any Old Company policyholder who does not assent to the Rehabilitation Agreement (for brevity called a *dissenting policyholder*) has the right to file his claim with the Commissioner (as Liquidator) and prove the damage he has suffered by the Old Company's breach of contract; and participate *pro rata* in the Liquidator's distribution of Old Company's assets in his hands (Ins. Code §1019-1025).

The substantial effect of the Rehabilitation Agreement is for New Company (with over $215,000,000* assets),

(*a*) To pay [100%] all Old Company's floating debt, and insurance liabilities (matured as of July 22, 1936) such as Death Claims, Disability Claims, Annuities, etc.;

(*b*) To assume [100%] all insurance liabilities (except Non-Can Policies);

(*c*) To assume [100%] all insurance liabilities under Non-Can policies—as to **Disabled** Lives—so as to pay [100%] all *past and future* Disability payments on account of disability which commenced prior to July 22, 1936;

(*d*) To assume Non-Can policy liabilities—as to **Active** Lives—to the extent of 20% to 90% of the benefits thereunder;

(*e*) To set aside certain funds and future Surplus earnings into the "**Special fund**" to be used towards ultimately paying [100%] benefits on all Non-Can Policies [**Active Lives** on July 22, 1936] with 3½% interest on the deferred restorations; and

(*f*) To pay the Liquidator (1) an amount equal to the **Reserves** established on July 22, 1936 by New Company for all policyholders who later became *dissenting* policyholders, and (2) a portion of the future profits.

*$223,000,000 on July 22, 1936.

Any *dissenting* policyholder can file his claim with the Liquidator; establish the amount of his damage for Old Company's breach of contract, according to whatever rules of law are applicable thereto; and participate in the Liquidator's distribution of all the funds in his hands among the claims filed with him—such funds consisting of (1) the Reserves, (2) further sums proportional to the "Special fund" just mentioned, (3) entire capital stock of New Company, and (4) any recoveries arising from wrongful acts of Old Company's officers, directors, etc.

The Rehabilitation Plan *did not compel* any policyholder to accept the Plan. If he rejected the Plan, he retained all his rights against the insolvent Company and its Liquidator. The Rehabilitation Plan thereby avoided questions which have arisen in various reorganization cases as to the power of a majority (no matter how large) to compel a minority (no matter how small) to consent to the majority's Rehabilitation Plan.*

IX. *Judicial approval of revised Rehabilitation Agreement.* On December 4, 1936, the Court (Willis, J.) entered the Order (sought to be reversed here by

*(See "Binding the Dissenter under State Reorganization Laws" 48 Harvard Law Rev. 1414-1428, and "State Control of Dissenting Minority Creditors in Municipal Debt Readjustments" 50 Harvard Law Rev. 946-956, for a full collection of laws and decisions thereunder; Shanks' "The Law of Railroad Reorganization as Affecting Institutional Investors" (1935) p. 328, 340; Mason's "Some Legal Phases of Bank Reorganizations" pp. 57, 60, *et seq.;* "Constitutionality of Recent Legislation Relating to Merger, Consolidation or Reorganization of Banks as Affected by Rights of Dissenting Creditors or Stock-holders," 92 A. L. R. 1337-1342, 96 A. L. R. 1445; Cf. Cardozo J.'s dissent in *Ashton* v. *Cameron Dist.*, 298 U. S. at p. 541.)

certiorari), which found and decreed, in substance, as follows:

(1) On July 22, 1936, Old Company's *liabilities* exceeded its *assets* [by about *eighteen million dollars*, R. 31]; and it "was in such condition that its further transaction of business would be hazardous to its policyholders, creditors and to the public"; its assets "would be of substantially less value if they were sold separately . . . than if they were sold as a going concern"; and its "intangible assets" as a going concern were worth "several million dollars" (R. 1385-6).

(2) The revised Rehabilitation Plan made "adequate provision" for "every class of policyholders, creditors and stockholders"; did not unfairly discriminate in favor of any class thereof; but "fairly and equitably" protected the rights of "all persons", and was "fair, just and equitable" (R. 1385-7).

(3) The "Rehabilitation Plan" was approved; its execution was authorized, together with any necessary or proper deeds or transfers of further assurance; and the past acts of the Insurance Commissioner as Conservator, in organizing New Company, and in carrying on Old Company's business *ad interim* as a going concern, were also ratified and approved* (R. 1378, 1387-8, 1392-5).

*A purported Oral Opinion of the Court (WILLIS, J.) and subsequent colloquy with Counsel, appears in the Record (R. 1469-1508), but it was not included in the Record as certified by the State Court Clerk; and the Supreme Court of California held that it was no part of the Record on Appeal and could not be considered a part of the Record (OPINION R. 1530).

X. *Appeal from the December 4th Order.* Nearly all of Old Company's 275,000 policyholders of every kind, have accepted the revised Rehabilitation Plan.* Only *four* persons, viz.: Mr. Neblett (holding one *Life* policy) and Messrs. Bettin, Dickinson and McDonald (each holding one *"Non-Can"* policy) appealed from the Order of December 4th—and they on the "Judgment Roll" alone, without any Bill of Exceptions, **so that none of the seven weeks' evidence was in the Record, which merely consisted of pleadings and orders** (R. 1445-6, 1457, 1468; OPINION R. 1517-8, 1526, 1529).

The appeal, therefore, presented nothing but bare questions of State and Federal law arising on the face of those pleadings and orders, with the conclusive presumption that the evidence established all the facts necessary to sustain the orders (OPINION R. 1528-1530, 1539, 1540, 1543; p. 40 note, *infra*).

Mr. Neblett, *et al.*, urged several Federal, and many *non*-Federal, grounds of attack, the latter being based on California's Constitution, statutes, and rules of local practice.

XI. *Supreme Court of California affirmed the December 4th Order; approved the Rehabilitation Plan; and authorized its execution and full performance thereunder.* **On December 7, 1937, upon oral arguments and elaborate Briefs (440 pages), the Supreme Court of California *affirmed* the judgment below—the reasons**

*As the Record closes with the December 4, 1936 order approving the Plan, it does not show the elections to accept (Cf. R. 1440); but the correctness of the above statement is easily shown by the Company's Annual Statements of December 31, 1936-1937 (Cf. Spectator Life Index 1938, p. 63).

for its rejection of each procedural and *non*-Federal ground of attack (with page references to the OPINION) being summarized in the margin† (*Carpenter* v. *Pacific Mutual,* 10 Cal. (2d) 307; R. 1509-1544).

†1. Insurance Commissioner could (without any prior Court Order) lawfully seize Old Company's assets and business, and organize a New Company to assist him in the operation thereof (R. 1527-8, 1533).

2. The five void orders (Edmonds, J., July 22-23), did not invalidate any subsequent orders by WILLIS, J. The latter stand by themselves independently of the prior void orders. (R. 1527).

3. WILLIS, J. (a qualified Judge), adopted, confirmed, ratified, and re-enacted the prior July 22 void order [appointing the Insurance Commissioner as Conservator] of the disqualified Judge (R. 1527-8).

4. WILLIS, J., validly and independently appointed the Insurance Commissioner Conservator (R. 1522, 1529).

5. Insurance Commissioner as Conservator [and without prior appointment as Liquidator, R. 1542] has power to form New Company (R. 1535), and then, with Court's approval to enter into a Rehabilitation Agreement with New Company (R. 1542), in order to take over the business of the insolvent Old Company (R. 1537-8); and the Rehabilitation Agreement here was within the contemplation of the California law, Sec. 1043 (R. *Id.*).

6. All of the Insurance Commissioner's *acts* were subsequently validly ratified and approved by WILLIS, J. (R. 1522, 1528, 1529).

7. The use of "Mutual" in New Company's corporate name was not fraudulent or improper (R. 1544).

8. Insurance Commissioner's subscription to New Company's stock did not violate California's Constitution (Ar. 12, Sec. 13) prohibiting the State from subscribing for corporate stock (R. 1543-4).

9. New Company's stock was validly issued; and even if Insurance Commissioner's "permit" were necessary, it is "conclusively presumed" to have been secured (R. 1542-3).

10. Insurance Commissioner (as Conservator) could convey assets of Old Company to New Company, even before his appointment as Liquidator (R. 1528-9, 1542).

11. Insurance Commissioner's transfer (as Conservator) of Old Company's assets to New Company did not violate California's "fraudulent conveyance" statute (R. 1536-7, 1541-2).

12. In an appeal (as here) on the "judgment roll," R. 1445, 1529, it is "conclusively presumed" that Findings of Fact were waived (R. 1530), a presumption that cannot be overcome by (*a*) inserting an uncertified purported colloquy (R. 1530; Cf. R. 1469-1508), or (*b*) an affidavit attached to a Brief (R. 1530); and,

That decision settles everything except the Federal grounds, viz. whether the December 4th Order (and the Rehabilitation Plan signed thereunder) violates the Federal Constitution's "due process" and "contract" clauses; which Federal grounds were likewise denied by the California Supreme Court (OPINION R. 1535, *et seq.*).

XII. *Certiorari granted.* Four policyholders (Mr. Nebiett, *et al.*) petitioned for *certiorari*, assigning many *non*-Federal grounds; but also specially claiming that the Rehabilitation Plan (carried out by State legislative authority† *Appleby v. Delaney*, 271 U. S. 403, 409) impaired the obligation of the "Non-Can" policy contracts, and denied "due process" to "Non-Can" policy holders, by removing Old Company's assets beyond subjection to their claims (Petition, pp. 13, 16-17; Brief, pp. 54-56).

On May 16, 1938, *certiorari* was granted (304 U. S.).

moreover, this was a "special proceeding" (R. 1530-1532) in which "Findings of Fact" are not required (*Id.*).

13. Old Company was insolvent not only on Dec. 31, 1935, but also on July 22, 1936 (R. 848, 999, 1001, 1385-6, 1528).

14. Rehabilitation (not liquidation) was necessary here (R. 1534-5).

15. In absence of any of the evidence on the seven weeks' trial, Court assumes that there was evidence to sustain trial Court's holding that there was no unfair discrimination (R. 1539-1541).

16. No evidence as to relative merits of different Plans (R. 1544).

17. As to equivalence of benefits given, Court assumes evidence sustains it (R. 1539).

†Cf. *Doty* v. *Love*, 295 U. S. 64, 71; *Milner* v. *Gibson*, 249 Ky. 594, 602; *Nagel* v. *Ghingher*, 166 Md. 231, 238, 240; *Re Mechanics Trust Co.*, 119 N. J. Eq. 141, 143; *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234, 238; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193; *Matter of People*, 264 N. Y. 69, 81.

XIII. *"Due process" in the procedural sense was abundantly given.* The four petitioners and all interested parties appeared and actively participated in the elaborate seven weeks'* trial in the lower State Court —with no objections or exceptions shown—and also in the appeal to the Supreme Court of California (R. 1451-1462, 1514-1516), which decided that the procedure followed complied with every statutory requirement (OPINION R. 1531-1537; *North Laramie Land Co.* v. *Hoffman,* 268 U. S. 276, 282).

In the light of those facts, there was no denial of "due process" in the *procedural* sense (*Davidson* v. *New Orleans,* 96 U. S. 97, 105; *Twining* v. *New Jersey,* 211 U. S. 78, 110; *American Surety Co.* v. *Baldwin,* 287 U. S. 156, 168; *Moore Ice Cream Co.* v. *Rose,* 289 U. S. 373, 384; *Standard Oil Co.* v. *Missouri,* 224 U. S. 270, 281, 287-8; *Dohany* v. *Rogers,* 281 U. S. 362, 365, 369; *Doty* v. *Love,* 295 U. S. 64, 70, 71).

Therefore, the "due process" ground is reducible to the assertion that California (1) has impaired the obligation of the "Non-Can" policy contracts, and (2) has thereby prevented the "Non-Can" policyholders from enforcing their alleged vested legal rights against Old Company's assets, all of which assets petitioners insist ought to be *immediately available* for subjection to the claims of Old Company's creditors (*Coombes* v. *Getz,* 285 U. S., at p. 448).

*Reasons 1, 2, 3, 6, 7 (Petition, pp. 12-15, 17-22) and Points A, B, C, D, E, F, G, H, I (Brief, pp. 33-53) are *non*-Federal; and they are foreclosed by the decision of the Supreme Court of California as matters of purely local law or statutory interpretation (*Standard Oil Co.* v. *Missouri,* 224 U. S., at p. 287; *North Laramie Land Co.* v. *Hoffman,* 268 U. S., at p. 282; *Dohany* v. *Rogers,* 281 U. S., at p. 365).

XIV. *Rights of policyholders under Liquidation and Rehabilitation.* Before considering Petitioners' grievances against the Rehabilitation Plan, it will be convenient at this place to note (1) the "measures of damage" applicable to the different groups of policyholders in the event of Liquidation, and (2) their rights on Rehabilitation.

Measure of Damages.

I. *In the event of liquidation:* The rights and liabilities of Old Company, its creditors, policyholders, shareholders, and all other persons interested in its assets, would be fixed as of the date of the Order of Liquidation "unless otherwise directed by the Court"; each claimant must file his claim with the Commissioner; each policyholder must establish his claim for damages for breach of contract, as of such date; receive his *pro rata* of the assets for distribution;* and the measure of damages for breach of his contract, by reason of the company's insolvency, is governed by the law of the place of performance.†

(1) In the case of *Life* policies, the *measure* of damages [governed by the law of California where the

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*Ins. Code §§1016-1021; 8 Couch on Insurance §2043, notes; 32 C. J., pp. 1039-1040; 5 Cooley's Briefs on Insurance (2d Ed.), p. 4676; *The American Casualty Ins. Company's case,* 82 Md. 535, 569-70; *North River Ins. Co.* v. *Walker,* 65 F. (2d) 116, 118; *People* v. *Commercial Alliance Life,* 154 N. Y. 95, 99-101; *Johnson* v. *Button,* 120 Va. 339, 343; *Commonwealth* v. *American Life Ins. Co.,* 162 Pa. St. 586, 589; *Lovell* v. *St. Louis Mutual Life Ins. Co.,* 111 U. S. 264, 274; *Carr* v. *Hamilton,* 129 U. S. 252, 256.

†2 Beale's Conflict of Laws §413.1; *Bell* v. *Lamborn,* 2 F. (2d) 205, 208; *Randolph Grocery Co.* v. *Lamborn,* 3 F. (2d) 139; Conflict of Laws Restatement, §413.

contract was to be performed, as the Old Company promised to make all payments at Los Angeles, Id.; *Ofield* v. *National Ben. Life Ins. Co.,* 293 S. W. 271, 273] is the value of the policy at the date of insolvency (8 Couch on Insurance, §2043; 32 C. J. 1039-1040; *Lovell* v. *St. Louis Mutual Life Ins. Co.,* 111 U. S. 264, 274-5; *Carr* v. *Hamilton,* 129 U. S. 252, 256), which value would be (*a*) at a minimum, the policy's cash surrender value, or (*b*) at a maximum, the excess of the present worth of future benefits over the present worth of future premiums expected to be paid viz. Reserve (*Garland* v. *Jefferson Standard Life Ins. Co.,* 179 N. C. 67, 73; *American Insurance Union* v. *Woodard,* 118 Okla. 243, 250-1; Nash's "The Measure of Damages upon Breach of a Life Insurance Contract" (1936) p. 709).

(2) In the case of *"Non-Can"* policies, the *measure* of damages* has not been considered by any Court.

I. For "Non-Can" **Disabled** Lives the measure would probably be the present value of the future disability monthly income expected to be paid according to the disability.

II. For "Non-Can" **Active** Lives three measures have been suggested—each widely different in principle and producing differences in amount, viz.:

*This measure of damages is also governed by the law of California. Mr. Neblett may claim that it should be governed by the law of the place where the contract was made; in which latter event, there would be forty-odd *different* "measures of damage," varying according to the laws of the forty-odd States in which contracts were made. Such a situation would result in intolerable delay, expense and trouble to determine the forty-odd *different* "measures of damage," to be applicable to the forty-odd *different* State groups of policyholders.

A. A *pro rata* part of the last annual premium—resulting in a *negligible sum,*—because of the *uncertainty* that a healthy policyholder will ever become disabled; and his consequent inability to establish any substantial damages.* If that is the correct "measure of damage," full payment of all claims for damages is available to everybody.

B. All premiums paid (with interest thereon from dates of payment)—a sum greatly in excess of the entire "Non-Can" Reserves as calculated by the Commissioner—based on an *erroneous analogy* to the rule in a few States in cases of *wrongful cancellation* of Life policies; a rule rejected in most States as inequitable, because it fails to consider or give credit for the *value of the protection* which the policyholder undoubtedly had up to the time of *wrongful* cancellation† (See *Mutual Reserve Fund* v. *Ferrenbach,* 144 Fed. 342, 344-346, for a full discussion and refutation; Nash *op. cit.,* p. 715).

**Loyal Friends of American Assn.* v. *Center,* 49 S. W. (2d) 898, 901 (Texas); *The American Casualty Ins. Company's case,* 82 Md. 535, 570; *Usher* v. *Sarco Co.,* 100 N. J. Eq. 428, 429-31; *Kipp* v. *Fidelity Title & Mortgage Co.,* 116 N. J. Eq. 409; *In re Mechanics Trust Co.,* 119 N. J. Eq. 141; *Johnson* v. *Button,* 120 Va. 339, 343; *North River Ins. Co.* v. *Walker,* 65 F. (2d) 116, 118 (C. C. A. 8th); *Smith* v. *Nat'l Credit Assn.,* 65 Minn. 283; *State* v. *Minn. Title Ins. & T. Co.,* 104 Minn. 447, 19 L. R. A. (N. S.) 639 note; *Vicars* v. *Mutual Benefit H. & Acc. Ass'n,* 259 Ky. 13, 17; *Phillips* v. *Pantages Theatre Co.,* 163 Wash. 303; Ins. Code, §§481, 10111; Civil Code, §3358.

†The conflicting rules as to the "measure of damage" in cases of wrongful cancellation of Life policies, are collected in 48 A. L. R. 110, *et seq.;* 107 A. L. R. 1235, *et seq.*

C. Value of the "Non-Can" policy at the date of insolvency, *i. e.*, excess of the present worth of anticipated future disability payments over the present worth of anticipated future premiums to be paid—both calculated upon some Disability Table [either that used in the calculation of the premiums or that adopted by the Commissioner in calculating the Reserve or by the Court in the liquidation proceedings]—which is much less than the Reserve on a "Non-Can" policy. The rule for applying this measure of damage, has been fully worked out in the case of *Life* policies—in the Federal Courts and in most of the State Courts (which have considered the subject)—and hence is easily adaptable to "Non-Can" policies (8 Couch on Insurance, §2043, notes 12, 13; 32 C. J. 1039, note 37; *Lovell* v. *St. Louis Mutual Life,* 111 U. S. 264, 374-5; *Carr* v. *Hamilton,* 129 U. S. 252, 256; *Mutual Reserve Fund* v. *Ferrenbach,* 144 Fed. 342, 345-6 (C. C. A. 8th), and cases there cited; *Garland* v. *Jefferson Standard Life,* 179 N. C. 67, 73; *American Ins. Union* v. *Woodard,* 118 Okla. 46, 248; *Ebert* v. *Mutual Reserve Fund,* 81 Minn. 116, 128. See annotations 48 A. L. R. 116; 107 A. L. R. 1237).

II. *In the event of Rehabilitaton:* Each policyholder has such rights as are accorded to him under whatever Rehabilitation Plan happens to be adopted by the California Insurance Commissioner (with the approval of the State Court).* This is so, because when an insurance company is in financial difficulties, the State, acting through its Insurance Commissioner, first

tries to remove the causes leading to these difficulties; if that be impossible, then to rehabilitate the business by some form of Rehabilitation Plan; and, only in the last resort, to liquidate the company's business (R. 1532-1534).

Such is California's public policy (OPINION R. 1532-1538).

SUMMARY OF POINTS DISCUSSED.

1. Mr. Neblett's right to object is limited to the effect of the Rehabilitation Plan on his Life policy; and he cannot question its validity as applied to "Non-Can" policies.

The Rehabilitation Plan (*a*) did not impair the obligation of Mr. Neblett's Life policy, and (*b*) did not deprive him of any property without due process of law. (pp. 31–43, *infra*)

2. "Non-Can" policyholders who were Disabled Lives on July 22, 1936, were re-insured 100%; and they have never objected to the Rehabilitation Plan.

The Rehabilitation Plan did not impair the obligation of the policies of such "Non-Can" (Disabled Lives). (pp. 44–46, *infra*)

3. The Rehabilitation Plan did not (1) impair the obligation of "Non-Can" Policies, on Active Lives, nor (2) deprive the holders thereof of their property "without due process of law."* Messrs. Bettin, *et al.*, have no just cause for complaint. (pp. 46-94, *infra*)

*We need not consider whether a Rehabilitation Plan may exclude a policyholder from his rights at law; because, in this case, if a policyholder did not care to assent to the Plan, it provided he should have his rights at law.

FIRST POINT.

I. Mr. Neblett's right to object is limited to the effect of the Rehabilitation Plan on his Life policy; and he cannot question its validity as applied to "Non-Can" policies.

II. The Rehabilitation Plan (*a*) did not impair the obligation of Mr. Neblett's Life policy, and (*b*) did not deprive him of any property without due process of law.

I. Mr. Neblett has only a single non-participating Ordinary Life Policy (No. 547,567). He does not have a "Non-Can" policy (R. 245, 1380, 1414, 1459, 1525).

Whatever Federal Constitutional grievance Mr. Neblett might have properly urged if he had been the owner of a "Non-Can" policy (and, as such, had also been one of the **Active** Lives), cannot be considered here, because he is limited to his *Life* policy and to the effect of the Rehabilitation Plan on himself and on *that* policy. He cannot appropriate for himself any grievance that "Non-Can" **Active** Lives may have on account of any *distinction in treatment* (i) between them and Non-Can **Disabled** Lives, or (ii) even between them and Life policies (such as Neblett's). This is so because the only person who can test the constitutionality of a State act is a person who is directly and adversely affected thereby; and he cannot espouse the cause of others differently situated.*

***Assaria State Bank* v. *Dolley*, 219 U. S. 121, 126 [Kansas Bank Guaranty law]; *Red River Valley Bank* v. *Craig*, 181 U. S. 548, 558; *Arkadelphia Co.* v. *St. Louis S. W. Ry. Co.*, 249 U. S.

II. Mr. Neblett's principal contention in the Trial Court was that the Rehabilitation Plan violated various provisions of California's Constitution and laws [R. 250-251, 1275—contentions entirely foreclosed here because decided adversely to him by California's highest Court, OPINION R. 1526-1544; pp. 22-24, *supra;* p. 34 note, *infra*].

Conceding [for argument's sake] that Mr. Neblett seasonably raised the Federal questions (*Gibbes* v. *Zimmerman,* 290 U. S. 326, 328), and that the Rehabilitation Plan adopted under Ins. Code, §1043, is an act of the State,* we must determine [A] whether it has deprived Mr. Neblett of his property "without due process of law," and [B] whether it has substantially impaired Mr. Neblett's means for the enforcement of his Life policy contract, or obstructed or derogated from his substantial contractual rights thereunder (*Hendrikson* v. *Apperson,* 245 U. S. 105, 113; *Home Bldg. & L. Assn.* v. *Blaisdell,* 290 U. S. 398, 430, *et seq.*).

Let us consider those claims in order:

[A] *"Due process" claim.* Mr. Neblett's voluntary intervention in the Rehabilitation proceedings, the

134, 149; *Hatch* v. *Reardon,* 204 U. S. 152, 160; *Aluminum Co.* v. *Ramsey,* 222 U. S. 251, 256; *Dahnke-Walker Co.* v. *Bondurant,* 257 U. S. 282, 289; *Hampton* v. *St. L. Iron Mt. & S. Ry.,* 227 U. S. 456, 469; *Arizona Employers' Liability cases,* 250 U. S. 400, 429; *Massachusetts* v. *Mellon,* 262 U. S. 447, 488; *Rindge* v. *Los Angeles,* 262 U. S. 700, 710; *Smith* v. *Cahoon,* 283 U. S. 553, 562; *Columbus & Greenv. Ry.* v. *Miller,* 283 U. S. 96, 100; *Carmichael* v. *Southern Coal Co.,* 301 U. S. 495, 513; Cf. *Hagar* v. *Reclamation District,* 111 U. S. 701, 712.

**C. B. & Q. R.* v. *Chicago,* 166 U. S. 226, 233; *Georgia Power Co.* v. *Decatur,* 281 U. S. 505, 508; *Grand Trunk Western R. Co.* v. *Railroad Co.,* 221 U. S. 400, 403; *Appleby* v. *Delaney,* 271 U. S. 403, 409.

seven weeks' judicial hearing and his active participation therein, his appeal to the Supreme Court of California, with his Briefs and Oral Argument, and that Court's elaborate consideration of all his contentions (R. 245, 1274, 1347, 1378, 1380, 1383, 1446, 1514), certainly satisfies every essential of *procedural* "due process," including jurisdiction of the person and subject-matter, a competent and impartial tribunal, notice, opportunity to be heard, full participation in the hearing, and elaborate consideration and decision by the State Courts (pp. 22-25, *supra*, and cases there cited).

The Supreme Court of California held that, under the California Insurance Code, (*a*) the Commissioner had the right summarily to seize the assets of Old Company, and to organize and use New Company as his agent in the administration of Old Company's affairs, and (*b*) the assets were validly transferred from Old Company to the Commissioner, and from him to New Company (OPINION R. 1528-9, 1541).* The California Court's interpretation of the California law, and its

*The Supreme Court of California said:

> "Here the transfer was made pursuant to a valid statute after court approval. . . . The commissioner, as already held, **validly took possession of the assets** of the old company on July 22, 1936. On August 11, 1936, he was **validly appointed conservator**, his prior acts approved, and his title to the assets expressly confirmed. By operation of law, pursuant to the express terms of the statute, **title to all of the assets of the old company became legally vested in the commissioner as trustee for all creditors. The transfer of these assets** from the commissioner to the new company **occurred pursuant to statutory authority and order of court.**"

decision that the procedure followed complied with all statutory requirements, is conclusive here.†

Therefore, the only question open is whether California had the power, consistently with the Fourteenth Amendment, to do what it did in the Rehabilitation of Old Company.

First: California's power to authorize its Insurance Commissioner to determine whether a California insurance company is insolvent, or in a hazardous condition, and, if so, summarily to seize all its assets, and to administer them, including the Rehabilitation of the business and the transfer of the assets to a New Company organized for that purpose under a Rehabilitation Plan, is surely as unassailable as is the well settled power of Congress to authorize the Comptroller of the Currency, through a Receiver appointed by him, to find out whether a bank is insolvent; and, if so, summarily to seize possession of all of its assets, and dispose of them by sale, or by reorganization under the Bank Conservation Act, under which (different from the California method) dissenting depositors and stockholders are bound by the provisions of the reorganization; and the Comptroller's determination of the grounds for seizure is final and conclusive.*

†*Standard Oil Co.* v. *Missouri*, 224 U. S. 270, 281; *Quong Ham Wah Co.* v. *Industrial Comm.*, 255 U. S. 445, 448; *North Laramie Land Co.* v. *Hoffman*, 268 U. S. 276, 282; *Midland Co.* v. *K. C. Power Co.*, 300 U. S. 109, 113.

*Act June 30, 1876 [19 Stat. 63] U. S. C. A. Title 12 §191; Bank Conservation Act March 9, 1933 [48 Stat. 2] U. S. C. A. Title 12 §§203, 207); *Kennedy* v. *Gibson*, 8 Wall. 498; *Casey* v. *Galli*, 94 U. S. 673; *U. S.* v. *Knox*, 102 U. S. 422; *Rosenblatt* v. *Johnson*. 104 U. S. 462; *Bushnell* v. *Leland*, 164 U. S. 684; Cf. *Forrest* v. *Jack*, 294 U. S. 158, 162, note; *O'Connor* v. *Watson*, 81 F.

Second: In its last analysis, Mr. Neblett contends that he has been deprived of "due process" because the Supreme Court of California has [as he thinks] *erroneously decided* (1) what the California Code permits the Insurance Commissioner to do, and (2) the effect of a *qualified* Court's adoption, ratification, and confirmation of the Commissioner's *acts* taken under prior void orders of a disqualified Judge—clearly *non*-Federal questions.

Mr. Neblett's claim that he has been deprived of his property "without due process" is, therefore, reducible to his contention that California has impaired the obligation of his Life policy (p. 25, *supra;* 2 Willoughby on the Constitution [2d Ed.] §781).

[B] ***"Impairment of Contract" claim.*** The Rehabilitation Plan offered to Mr. Neblett [and to all other policyholders, *except* "Non-Cans" on **Active** Lives only] ***two options,*** with full opportunity to make a deliberate choice between them (R. 1440, 1525-6), to-wit:

Options Open to Mr. Neblett.

(1) New Company, with about $223,000,000 assets* would re-insure and assume [100%] Old Com-

(2d) 833, 836; 9 C. J. S. Banks and Banking §§746-750; ***State Savings Bank*** v. ***Anderson,*** 165 Cal. 437, affirmed 238 U. S. 611; ***North American Bldg. Assn.*** v. ***Richardson,*** 6 Cal. (2d) 90, 98, 100; ***Wittnebel*** v. ***Loughman,*** 80 F. (2d) 222-225.

*Constituting entire assets of Old Company, except any claims arising from wrongful acts of former officers, directors, etc.

On Dec. 31, 1935 this was..........$215,000,000 (R. 22)
On July 22, 1936 this was.......... 223,000,000

pany's total liability under Mr. Neblett's policy (R. 1397-8, 1400, 1525); with maintenance of the full legal Reserve as required by Commissioner (R. 1409); no investment or re-investment of New Company's assets to be made without written approval of Commissioner (R. 1400); and acceptance to constitute a novation, thereby releasing Old Company from all liability under the assenting policyholder's policy;

Or,

(2) Neblett to file his claim with the Commissioner (as Liquidator and statutory successor of Old Company); to prove his damages for Old Company's breach of contract on becoming insolvent, according to such "measure of damage" as the California Courts should determine to be applicable (R. 1440 fol. 4319; R. 1422-3 fol. 4264, 4266, 4268; R. 1526; Ins. Code, §1016-1025, 1032); and then to participate proportionately (with all other policyholders rejecting re-insurance) in the payment of his claim out of

(*a*) *Cash equal to the Reserves* (established in accordance with the Commissioner's requirements) which New Company had established for those who became *non-assenting* policyholders [R. 1421-2 fol. 4263-4],

(*b*) New Company's future profits [R. 1422-3 fol. 4265-8; R. 1416 fol. 4247-8; Opinion R. 1525-6],

(*c*) New Company's $1,000,000 capital stock [with $2,000,000 cash Surplus; and with good will,

agency organization, and other intangible assets worth *several million dollars more,* R. 1404 fol. 4212; R. 1386; pp. 14-15, *supra*], and

(*d*) Anything realized from Old Company's claims arising from wrongful acts of its former officers, directors, etc. [R. 1397-8 fol. 4191, 4194].

The Rehabilitation Plan did not compel Mr. Neblett to accept its terms (R. 1422, 1440, 1525, 1538). *It merely made him an offer* (OPINION R. 1525, 1528).

* * * * * * * *

1. *If accepted,* the Plan gave him 100% preservation of all his present and future contract rights; and he could either

(1) Stop paying premiums and immediately receive the policy's full non-forfeiture Surrender Value *in cash,* or in "paid-up" or "extended" insurance, as he might prefer; or

(2) Continue paying premiums to keep his policy in force, with 100% re-insurance in, and assumption by, a solvent New Company, having (*a*) over $220,000.00 assets, and (*b*) full legal Reserve—a New Company relieved from much of the burdensome "Non-Can" liability which had caused Old Company's insolvency.

From a practical standpoint [whatever the "Non-Can" **Active** Lives might think about the effect on *their* rights], the Plan offered Mr. Neblett, as a *Life* policyholder, a perfect method for

(1) The immediate collection of his policy's *full cash surrender value; or*

(2) Keeping his insurance in force; and, in the latter case, the collection of the *full face of his policy* at its future [perhaps distant future] maturity

—neither of which methods would have injured Mr. Neblett in any way; but either method would have put him in a better position than he was already in as a policyholder in an *insolvent* company, which, if liquidated at forced sale, could not begin to make him whole, whatever his "measure of damage" might be held to be.

Therefore, the Plan did not impair the obligation of his contract when it offered him *something better* than he would otherwise get (*Bernheimer* v. *Converse*, 206 U. S. 516, 530).

2. Nevertheless, Mr. Neblett *rejected** the offer (as he had the right to do); but he cannot make that rejection the basis of a claim that California has impaired the obligation of his contract when it offered him the option just noticed (*Bernheimer* v. *Converse*, *supra*).

Mr. Neblett's rejection of the Plan left him with his full legal rights intact against the insolvent Old Company, to be enforced in accordance with the laws of California (Ins. Code, §1016-1027), to-wit: to file his claim with the Commissioner as Liquidator of Old Company, where it would be *allowed* (but not necessarily fully paid) in such an amount as the California Courts decided was the "measure of damage" against an insolvent Life Insurance Company, *i. e.*, the value of the policy on July 22, 1936.

*The Record does not *affirmatively show* a rejection. If Mr. Neblett prefers to appear as a *consenter* to the Plan instead of a *dissenter*, he may be so treated on this *certiorari*. But if so, the novation released the Old Company (R. 1441; OPINION R. 1538).

New Company agreed to pay such allowed claims, in the manner, and to the extent, as provided in the Agreement (R. 1526); and Mr. Neblett would participate with all other *dissenting* policyholders in the several different funds listed (pp. 17-19, 36-37, *supra*).

That also ensured him a full participation in the value* of Old Company's business as a "going concern," because the *entire capital stock* of New Company (which had taken over the profitable part of Old Company's business, assets and liabilities) **carried with it all the equity in the New Company,** and was held by the Commissioner "as trustee," for the benefit of *dissenting* policyholders (OPINION R. 1526, 1539), and Mr. Neblett would also participate in the other funds mentioned (pp. 17-19, 36-37, *supra*).

Did such a Rehabilitation Plan impair the obligation of Mr. Neblett's policy contract?

(*a*) Mr. Neblett urged the lower Court to direct a "*sale* of all the assets *within a limited time* to the highest and best bidder" (R. 1347-1349). As a creditor of an *insolvent* corporation, Mr. Neblett had no vested right [protected by the Federal Constitution] which would prevent California from changing the method, or offering an additional method, for the enforcement or collection of creditors' claims against an insolvent corporation (2 Willoughby on the Constitution [2d Ed.], §748; *Gibbes* v. *Zimmerman,* 290 U. S. 326, 332; "The Constitution of the United States does not confer upon the depositors a vested right of liqui-

*No part of which would he have received on liquidation.

dation at the hands of a state official," *Doty* v. *Love*, 295 U. S. 64, 70; *Dunn* v. *Love*, 172 Miss. 342, 354, 358; OPINION R. 1538).

(*b*) Who is to *determine* whether Mr. Neblett's Plan for an immediate sale of all the Old Company's assets to the highest and best bidder, was a *better method* than the Commissioner's Plan, for enforcing and collecting the claims of *Life* policyholders against an insolvent company [which is the only question he is entitled to raise, p. 31, note, *supra*)? **Obviously, some Court must make that decision.**

After a seven weeks' trial, the lower Court decided *against* Mr. Neblett's plea for liquidation, and *in favor of* the Rehabilitation Plan in controversy as the better plan (R. 1385-1387); and the Supreme Court of California affirmed that decision (R. 1541; pp. 57-8, *infra*).

Such was the decision of the California Courts on the facts.

(*c*) **In the absence* of any evidence whatever, this Court cannot find the facts differently from the State**

*In the absence of the evidence [*unless* the Rehabilitation Plan is *bad on its face*], the presumption of constitutionality prevails (*O'Gorman & Young* v. *Hartford Ins. Co.*, 282 U. S. 351, 358, notes 3, 4 and cases cited therein; *Fort Smith Light Co.* v. *Paving Dis.*, 274 U. S. 387, 391, 392; *Pacific States Co.* v. *White*, 296 U. S. 176, 185, 186; *Concordia Fire Ins. Co.* v. *Illinois*, 292 U. S. 535, 547-8; *Aetna Insurance Co.* v. *Hyde*, 275 U. S. 440, 447-8; *Hodge* v. *Cincinnati*, 284 U. S. 335, 338; *Milner* v. *Gibson*, 249 Ky. 594, 609: *Loftus* v. *Dept. of Agriculture*, 211 Iowa, 566; see "Questions of Fact Affecting Constitutionality," 38 Harvard L. R. 6).

The State Court's determination of facts is conclusive in this Court (*Penn Oil Co.* v. *Minnesota*, 248 U. S. 158, 164). It is especially true in California that, where an appeal is taken (as here) on the Judgment Roll alone, if, from the facts adjudged by the trial Court, other facts may be inferred to support the judgment, such other facts will be deemed to have been inferred

Court; and Mr. Neblett cannot prove (1) that he has been injured, or (2) that he would have been substantially better off, if the Court had liquidated all assets of Old Company and applied them to the payment of all claims that might be established under the various "measure of damage" rules which the California Courts might adopt respecting the breach of the various kinds of contract involved, or (3) that the Rehabilitation Plan's provision for New Company's 100% re-insurance and assumption of all Old Company's liability to Mr. Neblett [or his optional right to have his claim allowed and to participate in the assets of Old Company, pp. 37-39, *supra*], thereby substantially impaired his right to enforce, or his opportunity to collect, damages for breach of contract under his policy.

(*d*) Mr. Neblett *rejected* 100% re-insurance and assumption in the New Company; and he demands that Old Company's $223,000,000 of assets shall be sold and distributed, among himself and all other policyholders whose claims are established, as damages for the breach of contract upon the Old Company's insolvency on July 22, 1936.

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by the trial Court; and, on appeal, no fact will be inferred contrary to what the trial Court might possibly have inferred to support the judgment—as the trial Court's determination of facts should be used to uphold, and not to defeat, its judgment (*Anglo California Trust Co.* v. *Oakland Rys.*, 193 Cal. 451, 460-61; *Willett* v. *Schmeiser Mfg. Co.*, 82 Cal. App. 249, 252-3; *Breeze* v. *Brooks*, 97 Cal. 72, 77; *Malmstedt* v. *Stillwell*, 110 Cal. App. 393, 399; *Kelling Collection Agency* v. *McKeever*, 209 Cal. 625, 628. To the same effect *Cross* v. *Georgia Iron & Coal Co.*, 250 F. 438 (C. C. A. 5th); *Morrison* v. *Regus*, 22 F. (2d) 804, 805 (C. C. A. 5th); *General Finance Co.* v. *U. S.*, 45 F. (2d) 380, 381 (C. C. A. 5th); *Life & Casualty Ins. Co.* v. *City of Florala*, 63 F. (2d) 195, 197 (C. C. A. 5th); *Wiggins* v. *Burkham*, 10 Wall. 129, 132; *McConnell* v. *McChord*, 172 Ark. 21, 22; *Wilson* v. *Trent*, 238 Ky. 551, 552; *Prehm* v. *Kindig* (Iowa; unreported), 232 N. W. 812.

To that contention (*d*) we respond:

First: California has provided a short and summary method by which Mr. Neblett can establish the amount (in dollars and cents) of his claim for damages against Old Company;

Second: The State has the right (consistently with the Federal Constitution) (1) to avoid the expense, waste and reduced amount realized from assets sold in forced liquidation; (2) to adopt appropriate means of applying an insolvent corporation's assets to the satisfaction of its creditors' claims other than by liquidation; and (3) to adopt any method to that end, so long as it does not substantially impair a creditor's fair and equitable participation in the value of the Company's assets, considering all the complex factors which must be taken into consideration in the case of an insolvent corporation, with $223,000,000 assets, doing business in over forty States, with 275,000 policyholders, having hundreds, if not thousands, of different situations presented as to the "measure of damage" and the method of ascertaining the amount thereof, arising from the great variety of policy obligations outstanding.

California secured to Mr. Neblett an equitable participation in Old Company's assets:

A. *If he assented to the Plan:* By organizing New Company, transferring to it most of the assets of Old Company, and then requiring New Company to assume 100% of Old Company's obligation to Mr. Neb-

lett. Such a method certainly did not impair the legal obligation which the insolvent Old Company was under to perform its contract with Mr. Neblett.

B. *If he dissented from the Plan:* He would receive as much as, or more than, he would in Liquidation, for the Supreme Court of California held that under the Rehabilitation Plan the assets were *far greater* than they would have been on Liquidation (R. 1386; Opinion R. 1539).

If Mr. Neblett had included in the Record all the evidence adduced in the seven weeks' hearing, such evidence may have conclusively established that the Rehabilitation Plan gave him, *whether assenting or dissenting from the Plan, very substantially more* than he could possibly have received from a forced liquidation. At any rate it must be so assumed here (p. 40 note, *supra*; p. 72, *infra*).

If Mr. Neblett desired to show that the Plan was so unfair as to violate the Federal Constitution, he should have included the evidence, from which the factual situation could have been considered by the Supreme Court of California, and in turn by this Court. By failing to do so, he waived that point (Opinion R. 1543).

The judgment below should be affirmed so far as Mr. Neblett is concerned.

SECOND POINT.

"Non-Can" policyholders who were Disabled Lives on July 22, 1936, were re-insured 100%; and they have never objected to the Rehabilitation Plan.

The Rehabilitation Plan did not impair the obligation of the policies of such "Non-Can" (Disabled Lives).

On July 22, 1936, at 1 P. M., there were a great many "Non-Can" policyholders who had *already become disabled;* and such persons are technically called "Disabled Lives."

It is needless to discuss their Federal Constitutional rights, or their supposed grievances, if any, against the Rehabilitation Plan, because:

(1) Not a single* Non-Can *Disabled* Life has ever objected to, or attacked, the Rehabilitation Plan, or appealed from the December 4 order to the Supreme Court of California, or joined in the Petition for *Certiorari;* and, therefore, Mr. Neblett (*Life* policy) and Messrs. Bettin, Dickinson and McDonald (Non-Can *Active* Lives) cannot espouse the cause of Non-Can *Disabled* Lives as of July 22, 1936 (See authorities cited p. 31, note, *supra*);

(2) Under the Rehabilitation Plan, New Company reinsured and assumed [100%] all Old Company's liability under Non-Can policies where the *disability had commenced prior* to July 22, 1936; and agreed "to pay

*One policyholder [Rabinowitz] objected to the Plan's requirement that notice of disability must be given in accordance with the policy's terms (R. 1310).

all disability benefits under Non-Can Policies for disabilities commencing *prior* to" July 22, 1936 (R. 1412, 1413, 1415). New Company thereby assumed and agreed to pay [100%] all Old Company's liabilities under all Non-Can policies on *Disabled* Lives as of July 22, 1936, including (*a*) all Disability payments that were *past due* on July 22, 1936; as well as (*b*) all *future* monthly income Disability payments (pp. 16-19, *supra*). To secure its obligation to such Disabled Lives, New Company had over $223,000,000 assets, with the full Legal Reserve on all such Disabled Lives—which, as a matter of pure mathematical calculation, amounted to $20,000,000 (R. 29).

(3) A "Non-Can" Disabled Life also had the option—as did Mr. Neblett—of *dissenting* from the Plan, in which event he was given the same right, as was Mr. Neblett (pp. 36, 38, 41, 43, *supra*) *i. e.* to file his claim with the Commissioner; to prove his damages (for Old Company's breach of contract on becoming insolvent) according to such "measure of damage" as the California Courts should determine to be applicable; and then to participate proportionately (with all other *dissenting* policyholders) in the payment of his claim out of the several funds in the Liquidator's hands as listed above (pp. 16-18, 20, *supra*). But, as the Record does not reveal a single dissenting Disabled Life, we must assume that *all* Disabled Lives *accepted* the Plan; and, therefore, it is unnecessary to consider the grievances, if any, of "Non-Can" Disabled Lives (R. 1441 fol. 4322); as the novation released Old Company from all liability to them (R. 1441).

Consequently, the Rehabilitation Plan certainly did not impair the obligation of any Non-Can policy (where the holder was a *Disabled* Life on July 22, 1936) in an *insolvent* insurance company; nor deprive such a *Disabled* policyholder of his property without "due process of law"; because, in lieu of his claim for *damages* against an *insolvent* company, the State (1) assured to him 100% reinsurance and assumption of his claim for *past* and *future* benefits, in a thoroughly solvent New Company, or (2) preserved his right to file his claim, have it allowed at law, and paid out of a greater sum than liquidation would have produced.

On this *certiorari*, the controversy is thus limited to the rights of the Non-Can **Active** Lives.

THIRD POINT.

The Rehabilitation Plan did not (1) impair the obligation of "Non-Can" Policies on Active Lives, nor (2) deprive the holders thereof of their property without due process of law.

Messrs. Bettin, *et al.*, have no just cause for complaint.

Active Lives. On July 22, 1936, Messrs. Bettin, Dickinson and MacDonald [hereafter collectively and individually referred to as Bettin] were *Active* Lives, each holding one "Non-Can" policy (R. 626, 681, 690, 1233).

Messrs. Bettin, McDonald and Dickinson (having *"Non-Can"* policies only) objected on the ground that

the Plan "is not the best possible plan," and if adopted, would render their policies "practically worthless" (R. 626-630, 681-687, 990-995, 1233-1236; p. 40, *supra*).

The Rehabilitation Plan offered to Bettin (and to all other "Non-Can" policyholders who were *Active* Lives upon July 22, 1936) a free choice between these two alternatives, to-wit:

First: New Company's reinsurance and assumption of a *reduced* Benefit on all "Non-Can" *Active* Lives (without any increase in future premiums to be paid, R. 1415), as follows:

(1) Whenever an Active Life shall become a *Disabled* Life *after* July 22, 1936, New Company will *immediately* pay only from 20% to 90%* of the monthly

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*The differences in the percentages of "Non-Can" Benefits (which New Company assumed) resulted from a "horizontal" percentage reduction in the **reserve** (*i. e.,* net liability) which was required for each of the several "Non-Can" groups with different premium rates. The Old Company had from time to time [1921, 1926, 1929, 1931 and 1932] brought out its new "Non-Can" policies with progressively increased premium rates or more restricted benefits. Such horizontal reduction of *approximately the same percentage* of the **reserve** (*i. e.,* net liability) caused the differences in the percentages of the [20% to 90%] *Benefits* assumed, because the policyholders (of the more recently issued "Non-Can" policies) will pay *more* and *larger* premiums in the future than those of the earlier issued policies. The policyholders of these more *recently* issued policies will fully pay for the *additional* percentages of Benefits assumed.

If a uniform "horizontal" reduction had been made in the *Benefits,* there would *not* have been a uniform percentage reduction in the *net liability* (*i. e.,* Reserve) of the Company under the several different premium groups. Had the Benefits under these policies been reduced by a uniform "horizontal" percentage, then the more recently issued policies would receive benefits much *less* than what their premiums were paying for, with the inevitable result that those policyholders would discontinue; and, thus, the only policyholders left would be those paying a very inadequate premium for even the reduced benefits, so that a *second insolvency* would result.

Disability Income that Old Company had promised; which, in the case of Bettin would be (R. 1412-1415):

Bettin	35%	(R. 990-1, fol. 2970; R. 1414)
Dickinson	35%	
MacDonald. . . .	45%	(R. 1233, fol. 3699; R. 1414)

(2) New Company bound itself to transfer, from time to time, into a "**special fund**" New Company's funds available for its general corporate purposes (not reasonably required for its needs as a "going concern," p. 18, *supra*); such "**special fund**" to be applied to the payment of *additional* Disability Benefits to all "Non-Can" *Active Lives* who become Disabled Lives *after* July 22, 1936, to the end that all such Active Lives (becoming Disabled Lives) might ultimately receive full [100%] Disability Benefits, with 3½% interest upon the deferred restorations (R. 1387, fol. 4159; R. 1416-17);

Or,*

Second: To *dissent* from the Plan—[as Mr. Neblett did†]; in which event an Active Life was given the same right as was given to Mr. Neblett (pp. 35-38, *supra*), to-wit: to file his claim with the Commissioner; to prove his damages for Old Company's breach of con-

*The Plan allocated to every "Non-Can" *Active* Life substantially the same amount of assets whether he accepted or rejected the Plan. If he *accepted* the Plan, certain assets (*i. e.*, reserve) were placed behind his policy; and as future earnings accrued they would be added to those assets. If he *rejected* the Plan, precisely the same amount of assets would be turned over to the Liquidator, to-wit, (*a*) reserve, and (*b*) future earnings as they accrued (cf. R. 1410-1411, 1416-1417, 1421-1422).

†See p. 38 note, *supra*.

tract on becoming insolvent (according to such "measure of damage" as the California Courts ultimately determine to be applicable to a policyholder who was an *Active* Life on July 22, 1936); and then to participate proportionately (with all other *dissenting* policyholders) in the payment of his damage claim (so established) out of the several funds in the Liquidator's hands, as listed above (pp. 16-18, 20, *supra;* R. 1398, fol. 4193; Ins. Code, §§1019-1025; R. 1442, 1440).

As Bettin rejected† the Plan, he is a *dissenting* policyholder—entitled to all the remedies under this Second alternative.

* * * * * * * * * *

When the State winds up an *insolvent* business, it distributes the assets among the creditors, either (*a*) by converting the assets into cash by a forced sale, or (*b*) through some Rehabilitation designed to preserve the value of the business as a "going concern," so as to realize for the creditors the largest amount possible out of the assets.

The State has the right to administer the affairs of an *insolvent* corporation created under its own laws; and, in so doing, in order to avoid the waste and injury due to enforced liquidation* the State may, as a part of its police power, provide for the organization of a New Company to assume, in whole or in part, the obligations of the insolvent corporation, so as to prevent a

†See p. 38 note, *supra.*

**Van Schaick* v. *Title & Mortgage Guarantee Co.*, 264 N. Y. 69; *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234; *Dunn* v. *Love*, 172 Miss. 342; *Dickinson* v. *Saunders*, 129 Fed. 16, 17; Fletcher—Cyclopedia Corporations, Vol. 7, §4840.

race of diligence between creditors, in order that the largest possible amount may be realized out of the insolvent corporation's assets, to the end that all creditors, foreign and domestic, may share equitably, and that the assets shall not be dismembered and sacrificed at less than their fair value (*Clark* v. *Williard*, 292 U.S. 112; *Manigault* v. *Springs*, 199 U. S. 473, 480; *Union Dry Goods Co.* v. *Georgia Public Service Corp.*, 248 U. S. 372, 375; *Home Bldg. & Loan Assn.* v. *Blaisdell*, 290 U. S. 398; *Milner* v. *Gibson*, 249 Ky. 594, 606; *State Board of Milk Control* v. *Newark Milk Co.*, 118 N. J. Eq. 504; *State* v. *Farm & Home Savings & Loan Assn.*, 338 Mo. 313; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193; See also 2 Willoughby on Constitution [2d Ed.], §762; Vance's Interstate Aspects of the Liquidation of Insolvent Insurance Corporations (1935), pp. 343-4, 348-350, 352).

California determined to exercise its police power to that end.

Bettin's Theory that the "contract" clause prohibits the Rehabilitation Plan's application to "Non-Can" (Active Lives).

Bettin contends that California has "impaired the obligation" of his "Non-Can" (**Active** Life) policy because of (*a*) the *impossibility* for a dissenting "Non-Can" **Active** Life *to subject assets* which the Plan transferred to New Company, and (*b*) the Plan's *difference in treatment* between "Non-Can" **Active** Lives and all other policies.

Bettin insists* (1) that all assets should be *converted into cash* through a liquidating sale and then distributed to all creditors in *strict arithmetical proportion* to the amounts of their claims as ultimately ascertained; or (2) that if any Rehabilitation Plan be adopted to preserve the value of the business as a "going concern" [through re-insurance by a New Company organized for that purpose], all policies

*In Bettin's "Opening Brief" in the Supreme Court of California (p. 9), he insisted that the purpose of the California law was,

> "either [1] liquidate them [insolvent insurance companies] and pay out every one according to the value of their policies, and thus wipe out the company, or [2] to acknowledge all of the obligations of the company and conserve the assets and try to rehabilitate the company."

The trouble with that theory is, *First: Liquidation* would cause enormous losses and shrinkage in the value of the assets; and great expense and delay in paying off the policyholders, on account of the difficulty to ascertain judicially "the value of their policies," according to the particular "measure of damage" applicable to each; and, *Second:* Rehabilitation on the basis of 100% performance of all its obligations would leave the Commissioner in as insolvent a condition as the Company was when it became insolvent. When Old Company was $18,000,000 insolvent, the Commissioner could not rehabilitate the business without providing for the $18,000,000 deficit. This *was* provided for by the Plan adopted.

(Life and "Non-Can" alike) must be reinsured (i) *for 100%, or (ii) for exactly the same reduced percentage,* **utterly regardless of the fact** that the delay,† the necessity for such arithmetical *pro rata* distribution, and identic reinsurance of all policies (of widely different kinds and financial effect on a reinsuring company) would (*a*) cause *all* policyholders (including Non-Cans) to receive *less,* and (*b*) render it *impossible to rehabilitate* the business as a "going concern" (See pp. 60-63, *infra*).

Bettin's theory of the effect of the "contract" clause must be promptly rejected for the following reasons:

1. The Constitution of the United States does not confer upon the "Non-Can" *Active* Lives any vested right to compel a "forced sale" liquidation at the hands of the State (*Gibbes* v. *Zimmerman,* 290 U. S. 326, 332; *Dunn* v. *Love,* 172 Miss. 342, 354-8; *Doty* v. *Love,* 295 U. S. 64, 70; 2 Willoughby on Constitution [2d Ed.] §748; pp. 39-40, *supra*).

It is now well settled that in a business of a distinctly public nature or concern, every creditor takes his contract with the knowledge that, in the event of

†*Expense and loss resulting upon delay* is a major element in the case of an insolvent *insurance* company, different from the case of an ordinary commercial insolvency (where the creditors are, at most, only a few thousands, the amounts of whose claims are generally definite, and rarely require the determination or application of any "measure of damage"), because, in the case of an *insurance* company, (1) the number of its creditors runs into *hundreds of thousands* or *even millions,* and (2) the amounts of those numberless claims are dependent in *every instance* upon very varying "measures of damage," frequently disputed, and always requiring complicated actuarial computations.

the corporation's insolvency, the State may administer the assets, in a reasonable and practical manner, for the benefit of the creditors *as a whole,* even though some readjustments in strict legal rights are necessary, *provided that,* on the whole, the general corporate assets are devoted to the payment of corporate obligations without arbitrary favoritism or unjust preference; and that a small *minority* of creditors, by invoking the "contract" clause of the Federal Constitution, *cannot defeat* the State's administration of an insolvent estate under a Plan which produces real and substantial justice to all creditors (*Id.*).*

2. The Commissioner and the Lower Court [acting for the State] **decided against a forced sale** in liquidation, because (1) the Commissioner found that Old Company's Life, Accident and Health business was very profitable; that it had spent several million dollars in building up its agency organization, which, together with the Company's good will and "value as a going concern must be preserved" (R. 846-7, 850);

*See also *Home Bldg. & L. Assn.* v. *Blaisdell,* 290 U. S. 398, 428-430, 434-445, and cases there cited; *Rent cases,* 256 U. S. 135, 256 U. S. 170, 258 U. S. 142; *Van Schaick* v. *Title & Mortgage Guarantee Co.,* 264 N. Y. 69; *Re National Surety Co.,* 268 N. Y. S. 88; s. c. 264 N. Y. 473; *Savings Investment & T. Co.* v. *Associated B. etc. Co.,* 122 N. J. Eq. 95; *Milner* v. *Gibson,* 249 Ky. 594; *State* v. *Title Guarantee & Trust Co.,* 168 Md. 376; *McConville* v. *Ft. Pierce Bank,* 101 Fla. 727; *Priest* v. *Whitney Loan & Trust Co.,* 219 Iowa, 1281; *In re Mechanics Trust Co.,* 119 N. J. Eq. 141; *McSweeney* v. *Equitable Trust Co.,* 16 N. J. Misc. 193; *Shepherd* v. *Mt. Vernon Trust Co.,* 269 N. Y. 234; *State* v. *Farm & Home Savings Assn.,* 338 Mo. 313, 90 S. W. (2d) 93; *Eskew* v. *Buckhannon Bank,* 115 W. Va. 579, 177 S. E. 433; *Timmons* v. *Peoples Trust Co.,* 114 W. Va. 618, 173 S. E. 79.

See also 80 A. L. R. 1487; 92 A. L. R. 1337; 96 A. L. R. 1445; 99 A. L. R. 1217; 104 A. L. R. 1203, for collection of cases.

and (2) the Trial Court, after seven weeks' hearing, adjudged:

> "That the properties, assets and estate of [Old Company] would be of substantially less value if they were sold separately . . . than if they were sold as a going concern; that [Old Company] had on July 22, 1936, *intangible assets* consisting of good will, agency organization and going concern values, which were and are of great value, to-wit: of *several million dollars;* that the said [Plan] is designed to accomplish the preservation and conservation of said intangible assets, and that the same do now exist and will hereafter continue to exist in the hands of the New Company. . . . That said rehabilitation and re-insurance agreement . . . is fair, just and equitable . . . . That adequate provision is made . . . for each and every class of policyholders, creditors and stockholders . . .; that neither said agreement nor the plan therein embodied discriminates unfairly or illegally in favor of any class of policyholders, creditors, stockholders or other persons . . . [It] does fairly and equitably protect and adjust the rights, obligations and liabilities of all persons concerned herein . . . . is feasible, and that operations under said agreement are feasible" (R. 1385-1387).

The Supreme Court of California, after reciting those findings (R. 1519, 1523-4), pointed out that the several million dollars of intangible assets "would have been irreparably lost to the injury of all concerned" unless Old Company's business were promptly carried on (R. 1526); that "All these intangible assets would be lost if the Old Company were liquidated" (R. 1535) and that (R. 1539):

"All the dissenter [Bettin] is entitled to is the equivalent of what he would receive on liquidation"; that while "The record is also silent as to what the policyholders would have received in liquidation . . . the judgment roll discloses [that] under the approved plan **the assets are far in excess of what they would be on liquidation.** On these appeals, without the evidence before us, in support of the judgment, we must assume that evidence was introduced on these vital points and that such evidence demonstrated that **dissenters** under the plan **received as much or more,** as they would have received on liquidation. The order appealed from contains a recital that adequate provision is made in the plan for each class of policyholder. We must assume that such recital was amply supported by evidence" (R. 1539).

Bettin's proposed liquidating sale of Old Company's $223,000,000 assets,† (in order to convert them into cash for distribution among its creditors), would have caused (*a*) an enormous shrinkage in the values realized at such a sale however carefully conducted, (*b*) heavy expenses during the period of liquidation, (*c*) *destruction of millions of dollars* of value of good will and agency organization, (*d*) great delay in distribution on account of the necessity of determining the particular measure of damage applied to each policy, (*e*) liquidation expenses for the policyholders themselves in trying to establish their "measure of damage," and (*f*) irreparable injury to thousands of policyholders who had become *uninsurable* on account of their health, and would be unable, even when they

†P. 51, *supra.*

received payment of their claim for damages, to use it for the purchase of new insurance.*

In the absence of the evidence below (pp. 22, 40, *supra*) these obvious considerations justified the Commissioner and the California Courts in adopting a Rehabilitation Plan that (i) avoided these enormous financial losses, (ii) preserved intact the business as a "going concern" that it might continue to make profits for the policyholders in the future, and maintain unimpaired 100% insurance on 200,000 Life policyholders, as well as on many (number not shown) Non-Can *Disabled* Lives—at the price of only a *partial* immediate reduction in the reinsurance of Non-Can *Active* Lives (who might *never* become disabled), with (as the Court below decided) almost a certainty that they would ultimately receive 100%, if they should become disabled.

In the order of December 4 appealed from, and affirmed by the Supreme Court of California, it was specifically adjudged, on the basis of the seven weeks' evidence, that the Rehabilitation Plan afforded:

> "a feasible method of providing, within a reasonable time, **full restoration of the benefits under the non-cancellable income policies** of [Old Company] to the extent that the payment of such benefits is not initially assumed by the New Company . . . (R. 1387; OPINION R. 1540, 1544).

The California Courts have found—and there is no evidence to the contrary—that Bettin will receive *as*

**Van Schaick* v. *Title & Mtge. Guarantee Co.*, 264 N. Y. 69, 85, 93; *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234, 240; *Dunn* v. *Love*, 172 Miss. 342; *Dickinson* v. *Saunders*, 129 Fed. 16, 17 (C. C. A. 1st); *Christensen* v. *Merchants & M. Bank*, 168 Miss. 43, 57; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193, 198 Atl. 529, 532; *Cf. Doty* v. *Love*, 295 U. S. at p. 71.

much (or more) under the Plan as he would have received by liquidation (R. 1539). Therefore he has no cause to complain (*a*) that any right secured by the Federal Constitution has been denied him, or (*b*) that the obligation of his contract has been impaired (*Nagel* v. *Ghingher,* 166 Md. 231, 171 Atl. 65, 68; *Dunn* v. *Love,* 172 Miss. 342, 155 So. 331, 335, aff'd 295 U. S. 64).

3. We need not stop to inquire whether some other procedure for administering the affairs of the insolvent Old Company would have produced better results for Bettin than the Plan actually adopted, because the Record fails to show that such other procedure (if any) would have produced better results than the Plan adopted.

If Bettin bases his Federal claim upon the theory that the best possible Plan was not adopted, he ought to have included the evidence in the Record (OPINION R. 1517, 1540, 1543-4), so that the Supreme Court of California and this Court could determine for themselves whether the State had impaired the obligation of Bettin's policy by arbitrarily, fraudulently, or foolishly adopting a Plan, which gave him less than some other Plan (R. 1544).

The Supreme Court of California aptly said (R. 1541):

> "Some reference is made . . . to other plans of rehabilitation submitted to the trial court. The evidence as to the relative merits of the various plans is not before us. The record shows that the Commissioner and the trial court studied and gave consideration to all proposed plans, and found the one here approved to be the one best

fitted to protect and preserve the rights of all concerned. Obviously this court, without any evidence before it, cannot now determine the relative merits of any of the submitted plans."

4. Whenever a life insurance company's assets fall even *one dollar below* the amount of its mathematically calculated Reserve, the company is insolvent; and, by the laws of all the States, its business must be stopped, and its affairs administered (in one form or another), by the State.*

Old Company was about $18,000,000 short in assets in order to be technically solvent.

Upon Old Company's insolvency, from what source could it obtain the necessary $18,000,000 additional?

No one would *give* it. The State could not furnish it (California Const. Art. 12, §13; R. 1543). The stockholders would not, and doubtless could not, put it up. Premiums on its existing business could not be increased (R. 1535). Borrowing was both utterly *impossible* (for no one would lend it), and equally *useless* (even if possible), because a loan would simultaneously increase Old Company's liabilities by the exact amount of the loan, and it would still be as insolvent as before.

Faced with the impossibility of securing the neces-

*Cf. 1 Couch on Insurance, §244 (a), pp. 520-526; Smith's "Notes on Life Insurance" (3rd Ed. 1876), p. 111 *et seq.;* McCall's "Review of Life Insurance" (1898), p. 15 *et seq.;* Dawson's "Elements of Life Insurance" (2d Ed.), p. 136; Moir's "Life Assurance Primer" (2d Ed.), p. 162 *et seq.;* Gephart's "Principles of Insurance," p. 184 *et seq.;* Hutcheson's "Some Facts in the Development of Life Insurance in the United States," pp. 14-17.

sary $18,000,000, the State could only do one of two things,* to-wit:

(1) **Liquidate** Old Company; convert all its assets into cash as best it could; and ultimately divide the cash (less expenses) among the 275,000 policies, *arithemetically proportional* to the amounts of their respective legal claims as the Courts should find them to be;

Or

(2) **Rehabilitate** the business of Old Company.

For adequate reasons, the Commissioner and the Court decided *not* to liquidate (pp. 11, 40, 42, 49-50, 53-55, *supra*). Bettin has no cause for complaint on that account (OPINION R. 1538).

The only alternative was to Rehabilitate (pp. 11, 59, *supra*).

Rehabilitation was impossible if the $18,000,000 had to be raised, **as there was no one to furnish it.** No one would pay $18,000,000 into the insolvent Old Company, even for its business as a whole.

Consequently, the State decided that the only possible rehabilitation was by an $18,000,000 **reduction in the liabilities.** That would (*a*) preserve millions of asset values for the benefit of the policyholders as a whole, and (*b*) give them, even with a *reduction* in their strict policy rights, much *more* than they could possibly receive through a forced sale liquidation.

The Plan actually adopted did not violate the Federal Constitution. It was, as the California Courts

*It was impossible for the Commissioner to remove the causes of Old Company's insolvency, *i. e.*, the insufficiency of the premiums charged for "Non-Can"; as such premiums on existing business could not be increased (OPINION, R. 1534-5).

decided, both feasible and just, would pay more to the policyholders than forced-sale-liquidation, or than any other Plan suggested, and it will probably pay even the "Non-Can" Active Lives 100% of their policy rights (R. 1387; OPINION R. 1540).

5. Justification for the Plan's apparent difference in treatment between (1) the 100% unconditional assumption of Life policies and "Non-Can" (Disabled Lives) and (2) only 20%–90% unconditional assumption of "Non-Can" (Active Lives), with a future conditional assumption for the remaining 80%–10%.

Old Company was insolvent. Obviously, everybody could not be paid in full. Claims had to be scaled down to permit the profitable part of the business to continue, so as to realize enough from the future profits to pay off what had been scaled down.

The Plan might have made the *necessary reduction* in Old Company's liabilities [which New Company would unconditionally assume] by either of two methods, viz.: a "horizontal" or a "vertical" reduction; but it is easily shown that the "horizontal" reduction would have been worse than Liquidation.

"HORIZONTAL" AND "VERTICAL" REDUCTIONS OF LIABILITIES—COMPARATIVE MERITS.

A. *"Horizontal" reduction in Liabilities and Benefits to be paid.* The Plan might have reduced Old Company's liabilities by $18,000,000 [which would have made Old Company technically solvent] or by $20,-

000,000 or more [which would have made Old Company solvent and with some provision for operating surplus or contingency funds], by (1) a 10%, or larger, "horizontal" reduction in all of its liabilities, except claims preferred by statute (e. g., Federal Tax claims) [liabilities including $170,000,000 Life policy reserves and $45,000,000 "Non-Can" (Active and Disabled) Reserves]; and, simultaneously, (2) a consequent *reduction in Benefits* which New Company would pay upon Maturity, Death and Disability.

A "horizontal" reduction would have fallen so heavily upon the *profitable* part of the business (*i. e.,* Life policies), that the following *destructive consequences* would have ensued (OPINION R. 1540):

The Agency Force (unable to sell *new* Life policies in a Company already in default on its outstanding Life policies) would disintegrate; the Company would lose the millions of dollars' value in its Agency Organization and good will; and it could not earn the otherwise certain future profits from its Life business.

Life policies always pay considerably *larger premiums* than are necessary to cover the cost of Life insurance; Participating policies receiving back such over-payments in the shape of annual dividends (*Rhine* v. *New York Life,* 248 App. Div. 120, 124-7; affirmed 273 N. Y. 1, 6-8, 12-13, 16-17). Life policyholders would quickly perceive that, despite their own *overpayments,* their insurance benefits were being greatly reduced, solely for the benefit of the "Non-Cans,"—who had grossly *under-paid* and who would continue to *under-pay* at the expense of the Life policies. Consequently, Life policyholders would simply abandon a

company, operating under what they would justly feel was such an *inequitable* Rehabilitation.

Dreaded "adverse selection" would instantly become rampant—persons smitten on one cheek will not turn the other, *viz.*: *Healthy* policyholders cash in their policies, and insure themselves in other companies; while *sick*, unhealthy or otherwise un-insurable policyholders keep up their policies, cause an abnormally high mortality, and geometrically increase the financial burden on the Company. This would soon cause a *second insolvency,* because no company can exist with *sick* policyholders predominating, as it must have the normal average of healthy policyholders in order to continue in business (*New York Life Ins. Co.* v. *Statham,* 93 U. S. 24, 32).

Upon such second insolvency, an even greater loss would befall all "Non-Can" policyholders, because "adverse selection" would produce a far more ruinous insolvency than the one already suffered.

Furthermore, by the "horizontal" method of reduction, all "Non-Can" *Disabled* Lives [who on July 22, 1936, were disabled] would suffer an extremely heavy "cut" in the future monthly Disability Income payments—all for the supposed benefit of "Non-Can" *Active* Lives who might *possibly* become *disabled* in the future. In rehabilitating an insolvent corporation, the State may fairly consider the effect on the future insuring public, of the Plan's comparative treatment of (*a*) *disabled* persons and (*b*) others who are active and may *never* become disabled, in connection with the future valuable goodwill of the New Company.

This destructive effect of any "horizontal" reduction [in *liabilities,* and, simultaneously, in the *benefits* under Life policies] upon any Rehabilitation Plan designed to preserve a "going concern" business and several million dollars' value of intangible assets, was so obvious that a "horizontal" reduction **was never suggested in any of the various proposed Rehabilitation Plans or objections by the fifty-odd Intervening Petitions and Responses** (pp. 12, 13, *supra*). On the contrary, every objecting policyholder, who offered an alternative suggestion in the court below, embodied in his suggestion a *different treatment* for "Non-Can" *Active* Lives from that given the other policyholders (R. 914, 1056, 1172, 1348, 1350). Such difference in treatment could not be brought about by any "horizontal" reduction, but only by a *"vertical"* reduction, in liabilities, now to be considered.

B. *"Vertical" reduction in Liabilities and Benefits re "Non-Can" Active Lives.* The only alternative was a "vertical" reduction varying according to (1) the character of the policies involved, and (2) the effect upon the success of the Plan.

Ordinary commercial insolvencies are generally caused by a shrinkage in assets, which must be spread uniformly over all unsecured claims with no special difficulty in their immediate expression in dollars and cents; *whereas,* Old Company's insolvency* was due,

*Old Company's "vertical" insolvency arose from the fact that, while the Life business (with 200,000 policyholders, $600,-000,000 insurance in force, $170,000,000 Reserves and $5,500,000 Surplus accumulated from Life premium payments) was highly profitable and had paid annual dividends for many years, yet, at the same time, its "Non-Can" business (with about 50,000 policy-

not to a shrinkage in assets, but to an utterly *irregular increase in liabilities* as between two groups of policies —one profitable, the other extremely unprofitable— where the *amount* of the *provable* liabilities of the unprofitable policies would be ascertainable only after a lengthy judicial determination of the particular "measure of damage" applicable to each of the hundreds of thousands of claimants.

The Rehabilitation Plan, with a "vertical" reduction, had the great advantage and manifest justice of (*a*) preventing a shrinkage of assets and expense incident to liquidation; (*b*) saving millions of dollars in "going concern" and goodwill value; (*c*) preserving both Life insurance protection, and "Non-Can" *Disabled* Lives' Benefits intact; (*d*) continuing to earn substantial profits out of the profitable part of the business, to be later applied to the "Non-Can" *Active* Lives; and (*e*) placing the necessary immediate reduction in benefits upon those whose *under-payments had caused the insolvency* (R. 1535), instead of upon those whose *over-payments* had kept the Company afloat for many years (*Id.*)—all of which was provided for at the cheap price (*f*) of an immediate *graded reduction* in the benefits for "Non-Can" *Active* Lives who might *never* become disabled, *plus* the further assurance that the profits* of the business would be primarily devoted

holders, who had paid inadequate premiums, had built up no Surplus, but had created a $23,000,000 deficit) was not only insolvent, but with steadily increasing deficits ahead of it.

*To the possible suggestion that as Old Company made no profits of recent years, New Company cannot make profits, we respond (*a*) New Company has ceased to do the "Non-Can" business which brought about Old Company's disaster; and (*b*) the Rehabilitation Plan fully provided for the *entire* cost of the *reduced* benefits under "Non-Can" policies.

to restoring 100% Benefits to all the "Non-Can" *Active* Lives.

The necessary *reduction* was accomplished (1) by New Company re-insuring and assuming [only 20% to 90%] benefits under all "Non-Can" *Active* Lives, and (2) by the smaller Reserve required for such reduced benefits (R. 1413-1415, 1421, fol. 4263). The details of the reduction, which was with respect to "Non-Can" *Active* Lives only, are fully explained at pp. 17-19, 48, *supra;* and even that reduction was restored, in whole or in part, by New Company's agreement to devote all available profits toward 100% restoration of "Non-Can" *Active* Life reduced benefits (p. 17-18, *supra*).

The following considerations show the

Intrinsic Fairness of Rehabilitation Plan

In the first place, Old Company's stockholders get nothing. Their supposedly valuable ownership of Old Company was completely wiped out. Every dollar of Old Company's $223,000,000 of assets is devoted primarily and exclusively to pay Old Company's policyholders and other creditors [and New Company's new policyholders, who, of course, are fully paying their own way as they go, by their new premiums].

Therefore, we have only to consider whether the Rehabilitation Plan's *application* of the $223,000,000 of assets to Old Company's policyholders and creditors was an intrinsically *fair distribution* among the different kinds of claimants.

We submit:

(*a*) Speed in Rehabilitation was essential, because if the business were once interrupted for any material time, its value as a "going concern" and the millions of dollars of assets in Agency Organization and in "good will" would be lost forever to everybody. Consequently, any temporary subordination or postponement of strict legal rights was only on account of the greater advantage for all (including those whose rights were so subordinated or postponed)* [OPINION R. 1528-9, 1540].

(*b*) Life policyholders and Commercial Accident and Health policyholders always paid *more* than adequate premiums for their insurance protection; and any reduction in their benefits would have wrecked the Plan (p. 61, *supra*). In such an event, New Company would have been unable to secure the anticipated future earnings from the Non-Participating Life and Commercial Accident and Health policies. It is those earnings [and the Participating Life policies' surrender of a part of their own future annual dividends], which will be used to assist in restoring [100%] benefits to the "Non-Cans" (OPINION R. 1540).

(*c*) "Non-Can" *Disabled* Lives were 100% reinsured, solely to preserve the good will of the Company, because the sight of disabled policyholders, shorn of their monthly income for support, would undermine public confidence and prevent the Rehabilitation Plan from being a success.

**Nassau Smelting & Rfg. Wks.* v. *Brightwood Bronze Co.*, 265 U. S. 269, 272; *Application by Van Schaick*, 239 App. Div. 490; 29 Ill. Law Rev. 599, 564.

Non-insurance floating debts were paid in full, because the amounts were small, past due, and precisely known. If left unpaid, they would injure the Company's credit, and might subject it to judgments and dismemberment.

(*d*) "Non-Can" policies *never* paid adequate premiums, and that was the primary cause of Old Company's disaster; and yet the Plan assured 100% benefits to "Non-Can" *Disabled* Lives, and a high percentage of benefits to "Non-Can" *Active* Lives, *plus* future profits to be derived from the profitable Life and Commercial Health and Accident policies (R. OPINION 1540).

(*e*) This graded reduction in re-insurance or assumption of "Non-Can" *Active* Life Benefits was in direct proportion to the adequacy of the premiums such Lives were paying; and the benefits are not only *all* that were paid for, but are *more* than were paid for, *i. e.*, to the extent of the future profits derived from the profitable business.

(*f*) After providing for the Legal Reserves required for, [and paid by], the Life, Health and Accident policies (out of which alone future profits could be made to fully restore "Non-Can" *Active* Life Benefits), all the remaining assets were allocated to the Accident Department.

This was principally for the benefit of "Non-Can" *Active* Lives, who thereby received *all assets* not absolutely needed to keep the business as a "going concern," by which millions of losses in liquidation were

avoided, and future profits would be earned, primarily for the benefit of "Non-Can" *Active* Lives.

Any further (unconditional) increase in "Non-Can" *Active* Life Benefits could only be had through a corresponding reduction in benefits for Life policyholders; but that would automatically destroy the Company's business (p. 61-63, *supra*); involve several million dollars' loss in intangible assets; and prevent the success of the Rehabilitation Plan—with the result that *all* policyholders would be *worse off* than before.

(*g*) The assets were of greater value under the Plan than in liquidation. A dissenting "Non-Can" *Active* Life will receive as much, or more than, and quite as rapidly as, in liquidation (R. 1386; 1524-5, 1535, 1539, 1540).

In view of the great uncertainty as to what a "Non-Can" *Active* Life's "measure of damage" would be, as ultimately to be determined by California Courts, the Plan gave to both *assenting* and *dissenting* "Non-Can" *Active* Lives, (1) *far more* than they could possibly receive under *one* asserted "measure of damage," (2) *about the same* as they would get under *another* asserted "measure of damage," and (3) *much less* than would be allowed under *another* "measure of damage"; but even if *allowed*, (2) and (3) could *never* have been *fully collected* from the insolvent Old Company or its Liquidator.

Unless Messrs. Neblett, Bettin, *et al.*, can affirmatively show that they have been "substantially injured in ultimate results," and have "in fact been *actually hurt* by the reorganization and the plan thereof," they

have "no right to complain whether upon *constitutional* or statutory or administrative grounds." (*Dunn* v. *Love,* 172 Miss. 342; affirmed in *Doty* v. *Love,* 295 U. S. 64.)

(*h*) If Bettin complains that a Life policy gets 100% assumption, while a Non-Can Active Life gets only 20% to 90% assumption, we reply (1) that 100% assumption of *Life* policies was essential to prevent liquidation, (2) that "Non-Can" Active Lives get 20% to 90% assumption (if they become disabled), with every probability that it will be 100% by the time they become disabled, and (3) that the great difference between a Life policy's claim for insurance fully paid for, and a "Non-Can" Active Life's *contingent* claim for a *possible* Disability Monthly Income *which has never been paid for,* justifies the difference in the relative amounts assumed by New Company.

If Bettin, as an Active Life, complains that a *Disabled* Life gets more than he [Bettin] will get if he becomes disabled *hereafter,* we reply that the *Disabled* Life's claim *had* matured, the amount was definitely known, and the Plan provided for its full [100%] assumption, *whereas,* Bettin has no matured claim, but only a *contingent possibility* that he *may* become disabled; and even if so, there is the *further contingency* as to whether, and how long, he will live to attain the successive monthly periods when Disability Income Payments become due. His contingency, *upon a contingency,* is of so remote and speculative a character that it was utterly impossible, consistently with any Rehabilitation Plan that would be workable, to assume

[100%] the *doubly contingent* liability to him; for, if so, New Company would, *ipso facto,* be as insolvent as the Old Company—and this is so because it was the huge liability to *Active* Lives, with inadequate premiums to support them, that caused Old Company's downfall (OPINION R. 1540).

(i) If Bettin complains of discrimination in that the "Non-Can" *consenter* gets *too much,* we reply that Bettin could have the "too much" for himself by merely consenting to the Plan.

If Bettin complains of discrimination, on the ground that the Life policy *dissenter* got better treatment than he, we say he errs, because they were given precisely the *same* treatment, to-wit: to file their claims before the Commissioner, have them allowed according to the "measure of damage" applicable to a breach of their respective contracts, and then to have such claims so ascertained paid *pro rata* out of the assets in the hands of the Commissioner as liquidator of the Old Company (OPINION R. 1539).

(j) In response to Mr. Neblett's suggestion [Supplemental Brief, p. 22] that the Life policies were given, in effect, a priority over "Non-Can" *Active* Lives, when they were all creditors alike with claims upon a common fund, we say that the priority or preference (if it can be so called) was made, because, otherwise it would have been impossible to carry on the established profitable business of the Company. Based upon "business necessity," preferred payments may sometimes be made, where otherwise "the probable

loss would exceed the required payments" (*Moore v. Donahoe*, 217 Fed. 177, 182 [C. C. A. 9th].*

The Supreme Court of California pointed out that if the evidence had been included in the Record, it might well be shown that "if *life* policies were reduced so as to be equalized with Non-Can policies, such reduction would dangerously impair the possibility of writing new life insurance, which would ultimately disorganize and destroy the agency organization"; that "such reduction in life policies would cause lapses and surrenders in such policies, particularly of those still insurable in other companies, leaving only undesirable risks accepting the reduction" ["adverse selection," p. 62, *supra*]; that "equalization would produce less for the Non-Can policyholders than the plan adopted"; and that, therefore, "the difference in treatment can be justified on the theory that such difference was necessary not only to preserve life policyholders' rights but also the rights of Non-Can policyholders" (R. 1540).

*Payment by a receiver of a penalty of doubtful validity assessed by prison authorities; allowed in order to avoid the cancellation of a valuable (but cancellable) contract for convict labor (*Asheville Cigar Co.* v. *Brown*, 100 Ga. 171); Allowance to stockholders (among whom the new management of the company was included) in a reorganization proceeding, in order to preserve the interest and efficiency of that management (*Re Donashoe's Inc.*, 19 F. S. 441); Allowance to stockholders in a reorganization in order to induce them to contribute new capital essential to the enterprise; *Kansas City Ry. Co.* v. *Cent. Union Tr. Co.*, 271 U. S. 445, 455; Swaine's "Reorganization of Corporations; Certain Developments of the Last Decade," 27 Col. L. Rev. 901, ——; "Some Legal Phases of Corporate Financing, etc.," pp. 135, 154-155; Cf. Payment in full of one creditor in a bankruptcy composition, in order to induce him to advance funds to supply the consideration of the composition (*Zavelo* v. *Reeves*, 227 U. S. 625).

In an appeal on the judgment roll the evidence is not brought before the Appellate Court (R. 1539, 1540, 1543); and the California rule is well settled that if any evidence could have been introduced which would have sustained the judgment or order appealed from, it will be presumed that such evidence was introduced. The facts thus presumed to have been established by competent evidence in the trial court constitute the facts found by the California Courts under their well established procedure.*

That certain priorities or preferences may be granted, in order that the very persons subordinated may ultimately obtain more than they otherwise would, has long been recognized in this Court† [*Cf.* OPINION R. 1540-1].

In the case at bar, the Supreme Court of California has recognized and adopted that very principle, which this Court (and all the inferior Federal Courts) has enforced for so many years in railroad and industrial foreclosures. A principle, which has this Court's authority for its adoption, certainly cannot be so arbitrary, capricious or unreasonable as to offend the "contract" clause of the Federal Constitution.

**Carpenter* v. *Pacific Mutual*, 10 Cal. (2d) 307, 325, 336, 339-341; *McAulay* v. *Truckee Ice Co.*, 79 Cal. 50; *Pacific Investment Co.* v. *Ross*, 131 Cal. 8, 10; *Antonelle* v. *City Hall Commrs.*, 92 Cal. 228, 229; *Shindelar* v. *Hadacheck*, 88 Cal. App. 319, 320; *Cummings* v. *Howard*, 63 Cal. 503, 504; 2 Cal. Juris 867-8, 876-7; and all recitals of fact in the Court's December 4th order must be accepted as true (*Keeling Collection Agency* v. *McKeever*, 209 Cal. 625, 628; *Anglo-California Trust Co.* v. *Oakland Rys.*, 193 Cal. 451, 461; *Gray* v. *Gray*, 185 Cal. 598-9; *Pavillion Ice Rink* v. *O'Brien*, 60 Cal. App. 185-6).

†*Miltenberger* v. *Logansport Ry. Co.*, 106 U. S. 286, 310-312; *St. Louis Trust Co.* v. *Riley*, 70 Fed. 32, 37; *Gregg* v. *Metropolitan Trust Co.*, 197 U. S. 183, 187; *Carbon Fuel Co.* v. *Chicago C. & L. R. Co.*, 202 Fed. 172, 174.

The Rehabilitation Plan allowed an apparent immediate preference to Life policies, in order (1) to prevent lapses and surrenders on a wholesale scale, which would have reduced the volume of *profitable old* business; and (2) to secure a desirable volume of *profitable new* business. From the large volume of such profitable new and old business, sufficient profits would be made to restore the reduced benefits to the Non-Can Active Lives (R. 1387). Any reduction in the benefits on Life policies causing wholesale lapses and surrenders, would have produced "adverse selection," which would soon have caused a far greater loss to the policyholders as a whole (including "Non-Can" Active Lives) than the amount of the preference.

That temporary preference was balanced, not only by preserving the value as a "going concern," but (1) by the entire equity in the New Company ($3,-000,000 cash capital and surplus, agency organization, "good will," etc.), certain future profits, an amount equal to the legal reserve, and other special funds that were segregated for the benefit of the *dissenting* policyholders, and (2) by certain future profits being applied to restore 100% benefits to Non-Can Active Lives who *assented* to the Plan.

(k) Mr. Neblett insists [Supplemental Brief, p. 23] that the Supreme Court of California erred when it held that the dissenting policyholders *could* file their claims with a Liquidator; as [he insists] no Liquidator was appointed.

To that we respond that the Supreme Court of California decided that the Rehabilitation Plan contemplated that the Commissioner would be appointed

Liquidator, with whom dissenting policyholders were required to file their claims, and that the Liquidator "will receive, liquidate and pay all claims" out of the assets transferred to him (OPINION R. 1525-1526; 1542).*

Mr. Neblett constantly complains that the Supreme Court of California has *erroneously decided something*. Rightly or wrongly, it has decided that the *dissenting* policyholder does have a Liquidator with whom he can file his claim for damages, which the Liquidator must pay. If and when, on a proper record, Mr. Neblett shows that California has denied him the right to prove and collect his claim as a dissenting policyholder for damages, it will be time enough then to consider whether such action denied him "due process" of law; but, so far, the Supreme Court of California, instead of deciding what Mr. Neblett says it decided, *has actually decided precisely the opposite,* namely: that a Liquidator will be appointed with whom Mr. Neblett can file his claim, and by whom it must be paid (OPINION R. 1525).

*As the Record closes with the December 4, 1936, order, it does not show the appointment of the Liquidator. On January 18, 1937, the Insurance Commissioner was appointed Liquidator [Los Angeles Examiner, January 19, 1937, p. 3, columns 1-2; *Hutchins* v. *Pacific Mutual Life,* 20 F. Supp. 150, 151, Col. 2].

Federal Question Involved

Does the "contract" clause of the Federal Constitution prohibit California's adoption of this Rehabilitation Plan, simply because (1) it made a "vertical" reduction in "Non-Can" *Active* Life Benefits, and (2) it did not give *identic* re-insurance to *every kind* of policy? The Rehabilitation Plan enabled an *insolvent* business to be *successfully rehabilitated* for the ultimate great benefit of its 275,000 policy-holders as a whole, by which most of them can maintain their insurance protection 100% in force; and the rest will receive certainly as much as, and probably a great deal more than, they could obtain from a forced liquidation.

This is not the case of one party to an ordinary commercial contract as against the other party, with which contract neither the public nor the general welfare is particularly concerned. Neither has California tried to relieve one party at the expense of the other party; nor to prevent any part of a debtor's assets from being subjected to the claims of his creditors.

This is a case where California has attempted a constructive Rehabilitation of one of its own insolvent corporations, for the sole purpose of conserving its assets and preserving its business for the benefit of all its creditors, policyholders and the general public (Cf. *Treigle* v. *Acme Homestead Assn.*, 297 U. S. 189, 197; *Hopkins Savings Assn.* v. *Cleary*, 296 U. S. 315, 336-7).

The insolvent Pacific Mutual was a corporation of nation-wide activities engaged in the business of Life

Insurance which vitally affects the public interest—an enormous business where, in the United States alone, a comparatively few corporations have about *twenty-five billion dollars* of assets; have over 120,000,-000 outstanding policies, insuring *sixty-five million policyholders* for over *one hundred billion dollars;* with an annual income of nearly *four billion dollars;* paying out each year nearly a *billion dollars* in Death Losses, and an additional *billion and a half dollars* to policyholders in the shape of dividends, endowments, surrender values, disability and double indemnity accident payments,—so that (including the insured policyholders and the beneficiaries who ultimately will receive the insurance) there are about *one hundred million people* in the United States who are insured in, and as beneficiaries will collect their insurance from, about sixty life insurance companies.

A business of that size and peculiar character, where a few corporations have long-range executory contracts with more than *two-thirds* of our total population, is so affected with a public interest and the general welfare, that it is universally recognized as subject to the closest kind of State inspection, supervision and control.* Its solvency is absolutely necessary and of the

***German Alliance Ins. Co.* v. *Kansas,* 233 U. S. 389; *O'Gorman & Young* v. *Hartf'd Ins. Co.,* 282 U. S. 251, 257; *Hartford Acc. Co.* v. *Nelson Co.,* 291 U. S. 352; *Life & Casualty Co.* v. *McCray,* 291 U. S. 566, 570; *Levy Leasing Co.* v. *Siegel,* 258 U. S. 242, 246-7, and cases there cited; *Block* v. *Hirsh,* 256 U. S. 135, 155-7; *McConville* v. *Ft. Pierce Bank & Trust Co.,* 101 Fla. 727, 734; 1 Couch on Insurance, §§244-247, and 1937 Supplement (*Id.*); Annotations 36 A. L. R., p. 1512; 72 A. L. R., p. 1173; 14 R. C. L., p. 857, §25 and Permanent Supplement "Insurance," §25; 32 C. J., p. 981, *et seq.* Gephart's Principles of Insurance, pp. 233-255. Cf. material collated in dissenting opinion of Brandeis, J., in *Liggett Co.* v. *Lee,* 288 U. S. 517, 548-567.

greatest public concern in order to safeguard its economic structure upon which the good of all depends. From 65,000,000 to 100,000,000 people are deeply concerned in the reasonable safety of their long-range insurance protection, because, for the many, payment will not be made until the far distant future,—even though by the inherent nature of life insurance itself, some sorely needed payments will be made to-morrow for those few, unexpectedly visited by death and accident.

When those many millions of policy contracts were made, there was impliedly read into each the reservation of the State power to safeguard the vital interests of its people, even though its emergency exercise of that power might sometimes necessarily result in slight modifications or abrogations (generally temporary) of pre-existing contractual obligations, where vital public interests would otherwise suffer;* and this is so, because all contracts are made subject to what is commonly called the police power, which is simply the power reserved to the States by the 10th Amendment.†

**Blaisdell case*, 290 U. S. at p. 435, 444; *Savings Invest't & T. Co.* v. *Associated B. Co.*, 122 N. J. Eq. 95; *North Jersey Title Ins. Co.*, 120 N. J. Eq. 148; *Marcus Brown Co.* v. *Feldman*, 256 U. S. 170, at p. 198, and cases there cited; *Van Schaick* v. *Title & Mortgage Guarantee Co.*, 264 N. Y. 69; *Priest* v. *Whitney Loan & Trust Co.*, 219 Iowa, 1281.

†*Home Bldg. & Loan Assn.* v. *Blaisdell*, 290 U. S. 398, 434, 437-8, 440-2; *Marcus Brown Co.* v. *Feldman*, 256 U. S. 170, 198; *Levy Leasing Co.* v. *Siegel*, 258 U. S. 242, at 249; *Manigault* v. *Springs*, 199 U. S. 473, 480; *In re Mechanics Trust Co.*, 119 N. J. Eq. 141, 149; *Savings Investment & T. Co.* v. *Associated B. Co.*, 122 N. J. Eq. 95, 103, and cases there cited; *North Jersey Title Ins. Co.*, 120 N. J. Eq. 148, 163; *Milner* v. *Gibson*, 249 Ky. 594, 606, and cases there cited; *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234, 243; *Van Schaick* v. *Title & Mortgage Guarantee Co.*, 264 N. Y. 69, 83; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 1933, 198 Atl. 529, 532; *Dunn* v. *Love*, 172 Miss. 342.

It is well settled (*Blaisdell* case, 290 U. S. at 440-444), that the Federal "contract" clause does not prohibit those incidental and conditional restraints upon contract rights. This Court held that the State may, at times, prevent the immediate and literal enforcement of contractual obligations, where for the general good there must be some rational compromise between individual rights and public welfare.

For nine years [1929-1938], the United States has suffered an industrial, agricultural, financial and economic depression of such magnitude, that individuals, firms, corporations, municipalities, States and even the Federal Government itself, in order to protect their creditors and the general public as well as themselves, have secured legislative relief from their financial obligations, a few of which measures are mentioned in the margin.* Some of these Relief Acts have been held

*Bank Holiday March 6, 1933 (48 Stat. 1689-1691); Gold Hoarding Act and Bank Conservation Act, March 9, 1933 (48 Stat. 1) and Executive Orders thereunder; Gold Devaluation, May 12, 1933 (48 Stat. 52); Gold Clause Repeal, June 5, 1933 (48 Stat. 112); Gold Reserve Act of 1934 (48 Stat. 337); Gold Devaluation Proclamation, Jan. 31, 1934 (48 Stat. 1730-1); [*Norman* v. *B. & O. R. Co.*, 294 U. S. 240; *Nortz* v. *U. S.*, 294 U. S. 317; *Perry* v. *U. S.*, 294 U. S. 330; *Holyoke Power Co.* v. *Paper Co.*, 300 U. S. 324; *Smyth* v. *U. S.*, 302 U. S. 329]; Bankruptcy Act, §§75, 77, 77B; "Emergency Legislation in the Several States," March-June, 1933, American Life Convention Special Bulletin No. 262 and Supplement thereto; "Moratory Legislation," 46 Harvard Law Rev. 1061-85; "Constitutionality of Mortgage Relief Legislation," 47 Harvard Law Rev. 660-8; "Binding the Dissenter under State Reorganization Laws," 48 Harvard Law Rev. 1414-28; "State Control of Dissenting Minority Creditors in Municipal Debt Readjustment," 50 Harvard Law Rev. 946-956; "Impairment of Contracts," 35 Michigan Law Rev. 1003 note 13; "Mortgage Moratorium Held Unconstitutional because Emergency had Ended," 51 Harvard Law Rev. 1292; "Some Legal Phases of Bank Reorganizations," "The Law of Railroad Reorganization as Affecting Institutional Investors," and "Inter-State Aspects of the Liquidation of Insolvent Insurance Corporations" [Papers read before Association of Life Insurance Counsel, 1934-1935].

void,† and at least two so amended as to be held valid;‡ but most of them have been sustained on the ground of police power, emergency, previously unexercised reserve powers of the States, judicial change in the rigidity of the application of prohibitory restrictions, distinctions between changing the remedy and altering the substantive right, Bankruptcy power, etc.*

Regardless of whether or not a general economic "emergency" exists now (or at any time), if a very large insurance company becomes insolvent, whose liquidation would cause great loss to its policyholders and much damage to the public generally, a situation exists which calls for the State's exercise of its reserved power to prevent a destruction of values to the detriment of its people. (*Van Schaick* v. *Title & Mortgage Guarantee Co.*, 264 N. Y. 69, *per Lehman, J.*; *Shepherd* v. *Mt Vernon Trust Co.*, 269 N. Y. 234; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193).

The application of the "contract" clause to the Pacific Mutual's Rehabilitation should be made with those considerations clearly in mind.‡

†*W. B. Worthen Co.* v. *Thomas*, 292 U. S. 426; *Worthen Co.* v. *Kavanaugh*, 295 U. S. 56; *Louisville Bank* v. *Radford*, 295 U. S. 555; *Ashton* v. *Cameron County Dist.*, 298 U. S. 513.

‡*Wright* v. *Vinton Branch*, 300 U. S. 440; *Adair* v. *Bank of America*, 303 U. S. 350; *Wright* v. *Union Central Life*, 304 U. S. ——; *U. S.* v. *Bekins*, 304 U. S. 27.

**Home Bldg. & Loan Assn.* v. *Blaisdell*, 290 U. S. 398; *U. S. Mortgage Co.* v. *Matthews*, 293 U. S. 232; *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648; *Gold Clause Cases*, 294 U. S. 240-381; *Doty* v. *Love*, 295 U. S. 64; *City Bank Co.* v. *Irving Trust Co.*, 299 U. S. 433; *Kuehner* v. *Irving Trust Co.*, 299 U. S. 445; *Holyoke Power Co.* v. *Paper Co.*, 300 U. S. 324; *Richmond Corp.* v. *Wachovia Bank*, 300 U. S. 124.

‡*Blaisdell case*, 290 U. S. 398, at p. 440; *Manigault* v. *Springs*, 199 U. S. 473, 480-1; *Union Dry Goods Co.* v. *Ga. P. S. Corp.*, 248 U. S. 372, 375-6; *M[illegible]er* v. *Gibson*, 249 Ky. 594, 606; *State* v.

In the field of banking, insurance, railroads, utilities and other businesses which have long been recognized as of such a *quasi*-public nature as to justify State regulation, a great many reorganizations have taken place and have been upheld by the Courts.£

The Pacific Mutual Rehabilitation Plan provided for 100% reinsurance and payment of every kind of debt and obligation, *except only* "Non-Can" (*Active* Lives) which were given from 20% to 90% immediate reinsurance, with a postponed reinsurance of the balance, dependent upon the success of the Rehabilitation Plan and the profits that might be derived from

Newark Milk Co., 118 N. J. Eq. 504, 516, 519; *State* v. *Farm & Home Savings Assn.*, 338 Mo. 313, 321; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193; *Indiana* v. *Brand*, 303 U. S. 95, 108-9, and cases there cited; 2 Willoughby on the Constitution [2d Ed.], §762.

£*National Surety Co., In re*, 268 N. Y. S. 88; affirmed 264 N. Y. 473; *Van Schaick* v. *Title Mortgage & Guarantee Co.*, 264 N. Y. 69; *National Surety Corp.* v. *Nantz*, 262 Ky. 413; *Doty* v. *Love*, 295 U. S. 64; *McConville* v. *Ft. Pierce Bank & T. Co.*, 101 Fla. 727; *Jennings* v. *Fidelity & C. Trust Co.*, 240 Ky. 24; *Dorman* v. *Dell*, 245 Ky. 34; *Milner* v. *Gibson*, 249 Ky. 594; *Sweeny* v. *Jefferson Co. Bank's Reorg. Comm.*, 250 Ky. 187; *Becker* v. *Amos*, 105 Fla. 231; *Timmons* v. *People's Trust Co.*, 114 W. Va. 618; *Dunn* v. *Love*, 172 Miss. 342; *Eskew* v. *Buckhannon Bank*, 115 W. Va. 579; *Priest* v. *Whitney Loan & T. Co.*, 219 Iowa, 1281; *Bank of Murray* v. *Farmers' Bank*, 257 Ky. 251; *Nagel* v. *Ghingher*, 166 Md. 231; *Hoff* v. *First State Bank*, 174 Minn. 36; *Paul* v. *Farmers' & M. State Bank*, 187 Minn. 411; *Hagen* v. *First State Bank*, 180 Minn. 113; *Dorman* v. *Jones*, 257 Ky. 4; *Ex Parte Tennessee Valley Bank*, 231 Ala. 545, 166 So. 1; *Timmer* v. *Hardwick State Bank*, 194 Minn. 586; *Re Mechanics Trust Co.*, 119 N. J. Eq. 141; *Shepard* v. *Mt. Vernon Trust Co.* 269 N. Y. 234; *Corstvet* v. *Bank of Deerfield*, 220 Wis. 209, 263 N. W. 687; *State* v. *Title Guarantee & T. Co.*, 168 Md. 376; *North Jersey Title Ins. Co., In re*, 120 N. J. Eq. 148; *Savings Investment & T. Co.* v. *Associated B. & Co.*, 122 N. J. Eq. 95; *McSweeney* v. *Equitable Trust Co.*, 16 N. J. Misc. 193; *Christensen* v. *Merchants, Etc., Bank*, 168 Miss. 43; *State* v. *Farm & Home Savings Assn.*, 338 Mo. 313; *Cralle* v. *Louisville Title Company*, 244 Ky. 753.

its future operation. No policyholder was compelled* to consent to the Plan. If he dissented, he could establish the amount of his claim at law; and then the Commissioner, as Trustee for the dissenting policyholders, would pay the claim from the funds in the Commissioner's hands, consisting of the entire capital stock of the New Company [thus giving to the "Non-Can" (*Active* Lives) policyholders the entire equity in the New Company], the full Legal Reserve on all dissenting policies, as well as a certain proportion of the future earnings (Opinion R. 1541).

This Court must determine whether California's Rehabilitation Plan (1) falls on the side of those *many* cases in which Rehabilitation Plans have been sustained, or whether (2) it falls on the side of those *few* cases where Rehabilitation Plans have been held to violate the "contract" clause or other Constitutional prohibition (*Hessen Siak Shams* v. *Nebraska State Bank* (1931), 48 F. (2d) 894), distinguished in *Milner* v. *Gibson*, 249 Ky. 594, 603; *Ashton* v. *Cameron County Dist.*, 298 U. S. 513).

Review of Recent Authorities Upholding Similar Rehabilitation Plans.

The thirty-odd financial reorganization cases listed in the footnote on the preceding page 80, show how closely the Pacific Mutual Plan conforms to those which have been sustained by the Courts.

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*See p. 20 note, *supra*.

Pacific Mutual's Rehabilitation Plan did not try to compel a non-assenting policyholder to come in under the Plan, and it thereby avoided one difficulty in *Hessen Siak Shams* v. *Nebraska State Bank*, 48 Fed. (2d) 894. That case has been superseded by the *Blaisdell* case, 290 U. S. 398, and *Doty* v. *Love*, 295 U. S. 64.

A review of some of them shows that the same considerations which induced the Courts to sustain those Plans are abundantly present here.

In *Doty* v. *Love*, 295 U. S. 64, this Court sustained a Rehabilitation Plan. In 1930 a Mississippi Bank closed its doors; after two years of partial liquidation by the Superintendent of Banks, it re-opened under a 1932 Rehabilitation Statute [the closed bank will be called Old Bank; and, as re-opened, will be called New Bank].

The Plan, proposed by three fourths of the creditors and recommended by the Superintendent of Banks, was (after notice and hearing) approved by the Chancery Court. It provided substantially as follows:

(1) Certain old shareholders contributed $55,000 cash to the New Bank's capital, in consideration of their *release from $110,000 double liability.* The Old Bank's assets were turned over to the New Bank, respectively ear-marked (*i*) part to enable New Bank to pay 25% on the deposits, (*ii*) part to create a $45,000 surplus for the New Bank, and (*iii*) part into a pool to be managed and collected by the New Bank, and applied to pay the remaining 75% of deposits.

(2) New Bank paid in full all deposits of $5 or less; agreed to pay 25% of the deposits in installments out of ear-marked assets (*i*); to apply $7,500 a year out of earnings to create a $45,000 surplus, and, as it did so, the assets (*ii*) were to be turned into the pool. All the balance of the assets (*iii*) went into the pool.

Of the 5,000 creditors affected, two appealed to the Supreme Court of the State, which affirmed the Plan (172 Miss. 342). On appeal, this Court held that the statute merely changed the method of liquidation, as the Old Bank's assets were devoted to the payment of its debts; and if the New Bank turned out to be unsuccessful, such an "outcome is an unlooked for incident of a method of administration conceived to be more efficient than present sale and distribution"; that the majority of the creditors were not imposing their will on a minority, as the Plan was only effective if the Superintendent of Banks and the Chancellor thoroughly considered the whole matter, and, upon the hearing, approved the Plan as "wise and just."

This Court aptly pointed out that what was done was "for the protection of existing creditors" in that "collections are made more promptly and readily by a going concern than by one in liquidation", and that "a live bank is much more efficient than a closed one in selling parcels of real estate or in carrying them while unsold at profitable rentals" (p. 71).

The Court said, in language particularly applicable to the Pacific Mutual's Rehabilitation, that the effect of the Plan was (p. 72):

> "to make it possible for the bank to be reopened with the result to the creditors of economies and other benefits that would otherwise be lost; . . . that in all probability the moneys thus obtained as contributions to capital [from the old shareholders in exchange for release from double liability] could not have been collected by judgment and execution, and that the *depositors* would be the *gainers* by the substituted form of payment."

With respect to that release of double liability and the payment of small depositors in full, this Court said (p. 73):

> "In last analysis, then, the appellant's grievance, if they have any, is this and nothing more, that there was error of judgment to their prejudice in the approval of the plan with the compromise of liability as one of its important features. . . . The testimony as to the probable results of liquidation without the aid of a reopened bank was not contradicted or discredited. But the result would not be changed if the record in that respect were different. Error of judgment in the compromise of liabilities is not a taking of property or an impairment of contract in derogation of the restraints of the Constitution of the United States. . . . The Chancellor found by his decree that it would be more economical to pay these accounts in full [$5 or less] than to incur the bookkeeping expenses incidental to a calculation of percentages whenever dividends were paid to others. The objecting creditors have not been damaged by that feature of the plan."

This Court recognized that where an insolvent company's assets were devoted entirely to the payment of its creditors, various adjustments were permissible, in the general interest of realizing the greatest amount possible by re-opening the company.

For example: The Mississippi Bank's depositors were completely prevented from subjecting the Bank's assets to the *pro rata* payment of their demand claims as depositors, because (i) the depositors could only get 25% of their deposits paid in 5% instalments as certain

assets were collected; (*ii*) $45,000 of assets could only be made available to pay depositors at the rate of $7,500 a year *if* earned by the New Bank, while (*iii*) the remaining 75% of deposits could only be collected as the New Bank might realize on the pool assets.

On the other hand, the claims of policyholders against Pacific Mutual were not *demand* claims [except for cash surrender values], but were for *future insurance protection;* all of which was 100% assumed by the perfectly solvent New Company, except as to "Non-Can" Active Lives which had no immediate claim (until Disability occurred); and yet, from the assets furnished to the Liquidator, "Non-Can" Active Lives were allowed to collect quite promptly the amount (when established at law) of their claims for damages for breach of contract, arising from the Old Company's insolvency (OPINION R. 1539-1540).

It is obvious that [while in both cases the assets of the insolvent company were, in a sense, removed from immediate seizure and subjection by their creditors], the Pacific Mutual Rehabilitation Plan was far less drastic than the Mississippi Bank Plan, from the standpoint of creditors promptly realizing on their demands.

In 1932-33, New York adopted a statute entitled "Rehabilitation, Liquidation, Conservation and Dissolution of Delinquent Insurers" the constitutionality of which has been repeatedly sustained, and under which many reorganizations have taken place (New York Ins. Law, §400, *et seq.*, p. 2, *supra*). The California Rehabilitation Provisions were copied substantially from that New York Law (OPINION R. 1532). The leading

cases are *Van Schaick* v. *National Surety Co.,* 239 App. Div. 490, affirmed 264 N. Y. 473, and *Van Schaick* v. *Title & Mortgage Guarantee Co.,* 264 N. Y. 69.

As the Pacific Mutual proceedings and Rehabilitation Plan followed that of the National Surety Co., it will be useful to review the New York cases with some care.

National Surety case. In April 1933, National Surety Co. (hereafter called Old Company) was insolvent, with potential liabilities of billions of dollars on guaranties, real estate and fidelity bonds. On April 29, the Superintendent of Insurance took possession of all its assets and adopted a Rehabilitation Plan, under which he organized (as here) a New Company with $4,000,000 cash capital and surplus, supplied out of the Old Company's assets.

The best assets were transferred to the New Company, which assumed [100%] all of the *profitable* part of the business. The stock of the New Company was (as here) held by the Superintendent of Insurance as trustee for the benefit of the creditors. The less desirable assets were held by the two subsidiary companies for the benefit of certain creditors.

The New Company assumed all losses occurring *after* May 1 on certain selected lines of preferred risks; but expressly declined to assume any losses occurring *prior* to May 1, 1933, or any liability on guaranties of mortgage bonds or of bank deposits in closed banks. Two subsidiary corporations were also organized to deal with those guaranties and certain "frozen assets."

The Rehabilitation plan was bitterly attacked; but it was sustained on the ground that the State Superintendent of Insurance and the Court had the right to Rehabilitate, rather than to Liquidate, a distressed insurance company, because (p. 96),

> "While it is true that one creditor or a few creditors may not be entirely satisfied, numerous other creditors and those dealing with the National Surety Company will most likely be saved millions of dollars by the method of rehabilitation proposed by the Superintendent of Insurance. The plan suggested seems feasible and to be for the benefit of all concerned, especially the creditors, . . . The method of safeguarding the rights of the creditors of the National Surety Company may have required the formation of a new corporation so that a very valuable good will and profitable business might be saved from ruin and thus eventually materially aid the creditors of the company."

The basis of the decision was that the State might place great responsibility upon the Superintendent of Insurance, and the Court; and that any abuse of that power could be checked by Appellate proceedings.

The result was that the great business of the National Surety Company was preserved as a "going concern"; and in 1936 the stock in the New Company was sold for over *ten millions of dollars* [$10,031,000], which went to pay off creditors (*In re National Surety Co.,* 248 App. Div. 111; affirmed 272 N. Y. 613).

The National Surety case was affirmed by the Court of Appeals (264 N. Y. 473), on the authority of *Van Schaick* v. *Title & Mortgage Guarantee Co.,* 264 N. Y. 69, where a Rehabilitation Plan was approved, under

which bonds, mortgages and other securities deposited with a trustee to secure a bond issue, were required to be turned over to the Superintendent of Insurance for administration in such a way, that the holders of the interests secured by the bonds were not allowed to enforce their rights in strict accordance with the letter of their contracts.

In an elaborate opinion by LEHMAN, J., based largely on the *Blaisdell* case, 290 U. S. 398, the law was upheld, in order that mortgagors might not be compelled promptly to meet the obligations of the mortgages on their property. The decision was based upon substantially the same reasons that actuated the California Courts in providing for 100% assumption of Life policies, a lesser assumption of "Non-Cans", and with a qualified assumption of the balance.

The Court pointed out that the free liquidation of mortgage bonds would result in wide-spread ruin to mortgagors and wide-spread damage to mortgagees; that the situation affected the vital interests and economic welfare of the community; that while each holder was entitled to enforce the mortgage, yet general foreclosure of the vast amounts of mortgages would ruin the owners, and

> "might so demoralize the real estate market that the value of all mortgages would be diminished and the credit of insurance companies and savings banks destroyed. In spite of all this, the owner of a single certificate in a series has a contractual right to insist upon the enforcement of every contractual obligation in which he is interested and to refuse to accede to any impairment of such

obligation or agreement. **The statute was intended to meet that situation."**

The Court held that the postponement of the enforcement of contractual obligations or their temporary impairment was permissible, because of the imemdiate danger to the economic welfare and vital interests of the community. That was a far more drastic interference with the rights of private contract than in the case at bar.

In *Thrower v. Kistler,* 14 F. Supp. 217, the National Surety plan of Rehabilitation was sustained, because, in that way, the value of the business as a "going concern" could be maintained. While the New Company could not assume the liabilities of the Old Company which had already matured, yet the New Company's stock was held for the benefit of the Old Company's creditors—just as here the $3,000,000 capital and surplus, and the "several millions of dollars" of agency organization, goodwill, etc., of New Pacific Mutual are held by the Commissioner for the benefit of all "Non-Can" (*Active* Lives) policyholders.

The respective assumptions of National Surety and Pacific Mutual, were largely the *converse* of each other. The New National Surety assumed all *future* losses, but *not* past losses; the New Pacific Mutual assumed all *past* and *future* losses, *except* only *future* "Non-Can" Active Lives. Otherwise, the two Plans were substantially the same. **In each case, certain kinds of policyholders were temporarily preferred over other policyholders; a preference which was balanced, however, by the total equity of the company being held for**

the benefit of those policies which were subordinated.

In *National Surety Co.* v. *Nantz,* 262 Ky. 413, the validity of the National Surety Rehabilitation was fully considered. It was held (1) that under the "full faith and credit" clause, the decision in New York was binding, and (2) that *intrinsically* the Rehabilitation was in line with similar rehabilitations in Kentucky, saying (p. 421);

> ". . . in liquidations of the affairs of extensive business interests, through and by legal proceedings the laws under which they are had and done will be liberally construed so as, if possible, to give effect to plans and methods of settlement that will ultimately result in the greatest benefit to creditors and other interested parties, even though usual remedies may be superseded or the enforcement of rights postponed, **and especially so when such departures are clearly shown to be beneficial rather than detrimental to the beneficiaries of the assets being administered; they are not to be interpreted as contravening the due process clause of either the Federal or State Constitutions but as affecting only procedural remedies and not substantive rights,"** citing *Northern Pacific Ry. Co.* v. *Boyd,* 228 U. S. 482, and *Doty* v. *Love,* 295 U. S. 64.

In *Milner* v. *Gibson,* 249 Ky. 594, a bank closed, and the Banking Commissioner took charge of all its assets. Subsequently a Reorganization Act was passed. Three-fourths of the depositors proposed a plan of Reorganization under which the re-opened bank agreed to pay in full all deposits less than $25; to pay 10% of

all deposits of over $25; and to pay the remainder in various instalments.

Dissenting depositors attacked the plan.

The plan was upheld largely upon the ground that there was nothing to show that ordinary liquidation would produce *more* for the depositors, in a shorter time, than provided for in the Reorganization plan. The basis of the decision was that, as banks fell within the police power, the State could provide for their reorganization even though it interfered incidentally with some contract rights.

In *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234, a bank was closed during the Banking Holiday. Under a subsequent statute, it was re-opened, with the consent of a large majority of the depositors and stockholders, under a plan by which the general deposits were reduced by 45%. On the authority of the *Blaisdell* case, the statute and plan were sustained upon the ground that it was beneficial to all directly concerned, even though it did change, in some degree, the contractual obligations of the parties. The Court said:

> "The statute was intended to prevent a small minority from blocking a fair and equitable plan of reorganization which has received the consent of the majority of those interested and the approval of an informed court after a hearing. Undue insistence upon strict performance of a contractual obligation may be unfair to others and may be opposed to the general welfare."

In *State* v. *Title Guarantee & Trust Co.*, 168 Md. 376, a bank reorganization provided for the stockholders to pay in a certain amount in satisfaction of their statu-

tory liability and to be released from the balance; the depositors to get 30% in cash, and to get the remaining 70% in certificates of a holding company to liquidate certain assets of the failed bank. Any dissenting depositors or creditor might apply to the court "for the ascertainment of the fair liquidating value of his claim." The plan was upheld.

In *Priest* v. *Whitney Loan & Trust Co.*, 219 Iowa, 1281, a statutory reorganization plan was agreed to by depositors having over 75% of the deposits, under which they took new certificates of deposit in the reorganized bank for 50% of the original deposits, to be paid in instalments over three years; the remaining 50% to be paid from earnings, from some poorer assets of the bank as reorganized, and from amounts paid in by the stockholders. The Court held that this was not an impairment of the obligation of the depositors' demand contract with the bank; but that it was the exercise by the State of its police power over a business affected with the public interest. The case contains a most elaborate review of all the authorities on the subject. The Court said:

> "* * * it has been universally held by courts of last resort everywhere that contracts made with institutions such as banks affected with a public interest are likewise inherently subject to the paramount power of the sovereign state, the people—the reserve power, sometimes called the police power, to enact, through the Legislature, additional remedial legislation in the public interest, affecting the supervision, regulation, control, or *liquidation* of banking corporations."

It is needless to review all the cases cited (p. 80 note, *supra*). They deal with banks, building and loan association, etc., which, under a variety of circumstances, were closed during the depression, generally during the March 1933 Bank Holiday declared by the President. Later, when State Rehabilitation Statutes were passed, the companies were reorganized under one of several different general plans, such as (*i*) "freezing" a part of the deposits for different periods of time, gradually to be paid out of assets as they were converted into cash; and (*ii*) the organization of a new company or the reorganized old company, by which the payment of a part of the old company's obligations was assumed, to be paid out of the old company's assets as liquidated; the balance of the obligations to be paid out of certain assets which the new company undertook, as agent, to liquidate for the benefit of creditors.

Those reorganizations were sustained, upon the general theory that such corporations were affected with the public interest; that the State had wide powers over their regulation while solvent, and even wider powers when they became *insolvent;* that the State could provide the conditions under which they should be liquidated or reorganized, including the right to postpone for the time being the immediate enforcement of contract rights—sometimes substituting stock for a percentage of the demand deposits; all upon the theory that the creditors, *as a whole,* would fare much better under a plan that would preserve the "going concern" value of the business, and provide a better liquidation of assets, than by a forced sale in liquidation.

The Courts held that great weight should be given to the determination of the State Banking Superintendent or Insurance Commissioner, and the judgment of the lower Court, when supported by a large majority of the creditors, as to the best course to pursue for the benefit of the creditors *as a whole;* and that incidental postponement of the right to subject the assets to the payment of creditors and some necessary priorities, were proper, [as exercised under the reserved power of the State to which every depositor or creditor was subject when he became a creditor]; and that such actions did not "impair the obligation of contracts" within the sense of the Federal Constitution.

The judgment of the Supreme Court of California should be affirmed.

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October 10, 1938.

[See Appendix for relevant California statutes]

APPENDIX

APPENDIX.

[Insurance Code of California (1935).
Article 14 Amended by Ch. 291 Stats. 1935]

Article 14. Proceedings in Cases of Insolvency and Delinquency.

1011. Upon the filing, by the commissioner, with the superior court in the county in which is located the principal office of such person in this ~~State, of a verified~~ application showing any of the following conditions to exist:

(a) That such person has refused to submit its books, papers, accounts, or affairs to the reasonable inspection of the commissioner or his deputy or examiner.

(b) That such person has neglected or refused to observe an order of the commissioner to make good within the time prescribed by law any deficiency in its capital if it is a stock corporation, or in its reserve if it is a mutual insurer.

(c) That such person, without first obtaining the consent in writing of the commissioner, has transferred, or attempted to transfer, substantially its entire property or business or, without such consent, has entered into any transaction the effect of which is to merge, consolidate, or reinsure substantially its entire property or business in or with the property or business of any other person.

(d) That such person is found, after an examination, to be in such condition that its further transaction of business will be hazardous to its policy holders, or creditors, or to the public.

(e) That such person has violated its charter or any law of the State.

(f) That a certificate of authority of such person has been revoked under section 10711.

(g) That any officer of such person refuses to be examined under oath, touching its affairs.

(h) That any officer or attorney-in-fact of such person has embezzled, sequestered, or wrongfully diverted any of the assets of such person.

(i) That a domestic insurer does not comply with the requirements for the issuance to it of a certificate of authority, or that its certificate of authority has been revoked;

Or, upon the filing, by the commissioner, of a verified application accompanied by a certified copy of the commissioner's last report of examination of any person to whom the provisions of this article apply showing such person to be insolvent within the meaning of Article 13, Chapter 1, Part 2, Division 1 of this code, said court shall issue its order vesting title to all of the assets of said person, wheresoever situated, in the commissioner or his successors in office, in his official capacity as such, and directing the commissioner forthwith to take possession of all of its books, records, property, real and personal, and assets, and to conduct, as conservator, the business of said person, or so much thereof as to the commissioner may seem appropriate, and enjoining said person and its officers, directors, agents, servants and employees from the transaction of its business or disposition of its property until a further order of said court.

1012. Said order shall continue in force and effect until, on the application either of the commissioner or of such person, it shall, after a full hearing, appear to said court that the ground for said order directing the commissioner to take title and possession does not exist or has been removed and that said person can properly resume title and possession of its property and the conduct of its business.

1013. Whenever it appears to the commissioner that any of the conditions set forth in section 1011 exist or that irreparable loss and injury to the property and business of a person specified in section 1010 has occurred or may occur unless the commissioner so act immediately, the commissioner, without notice and before applying to the court for any order, forthwith shall take possession of the property, business, books, records and accounts of such person, and of the offices and premises occupied by it for the transaction of its business, and retain possession subject to the order of the court. Any person having possession of and refusing to deliver any of the books, records or assets of a person against whom a seizure order has been issued by the commissioner, shall be guilty of a misdemeanor and punishable by fine not exceeding one thousand dollars or imprisonment not exceeding one year, or both such fine and imprisonment.

1014. Whenever the commissioner makes any seizure as provided in section 1013, it shall, on the demand of the commissioner, be the duty of the sheriff of any county of

this State, and of the police department of any municipal corporation therein, to furnish him with such deputies, patrolmen or officers as may be necessary to assist the commissioner in making and enforcing any such seizure.

1015. Immediately after such seizure, the commissioner shall institute a proceeding as provided for in section 1011 and thereafter shall proceed in accordance with the provisions of this article.

1016. If at any time after the issuance of an order under section 1011 it shall appear to the commissioner that further efforts to proceed under said section would be futile, he may apply to the court for an order to liquidate and wind up the business of said person. Upon a full hearing of such application, the court may make an order directing the winding up and liquidation of the business of such person by the commissioner, as liquidator. The title to all property and assets of such person, vested in the commissioner under section 1011, shall remain in the commissioner, as liquidator, for the purpose of carrying out the order to liquidate and wind up the business of such person.

1019. Upon the issuance of an order of liquidation under section 1016, the rights and liabilities of any such person and of creditors, policyholders, shareholders and members, and all other persons interested in its assets shall, unless otherwise directed by the court, be fixed as of the date of the entry of the order in the office of the clerk of the county wherein the application was made.

1021. Upon the making of an order to liquidate the business of such person, the commissioner shall cause to be published notice to its policyholders, creditors, shareholders, and all other persons interested in its assets. Such notice shall require claimants to file their claims with the commissioner, together with proper proofs thereof, within six months after the date of first publication of such notice, in the manner specified in this article.

1024. Unless such claim is filed in the manner and within the time provided in section 1021, it shall not be entitled to filing or allowance, and no action may be maintained thereon. In the liquidation, pursuant to the provisions of this article, of any domestic insurer which has issued policies insuring the lives of persons, the commissioner shall, within thirty days after the last day set for the filing of claims, make a list of the persons who have not filed proofs of claim with him and to whom, according to the books of said insurer, there are amounts owing under

such policies, and he shall set opposite the name of each person the amount so owing to such person. Each person whose name shall appear upon said list shall be deemed to have duly filed, prior to the last day set for the filing of claims, a claim for the amount set opposite his name on said list.

1025. Claims founded upon unliquidated or undetermined demands must be filed within the time limit provided in this article for the filing of claims, but claims founded upon such demands shall not share in any distribution to creditors of a person proceeded against under section 1016 until such claims have been definitely determined, proved and allowed. Thereafter, such claims shall share ratably with other claims of the same class in all subsequent distributions.

An unliquidated or undetermined claim or demand within the meaning of this article shall be deemed to be any such claim or demand upon which a right of action has accrued at the date of the order of liquidation or accrues within the time limit provided in this article for the filing of claims, and upon which the liability has not been determined or the amount thereof liquidated; provided, however, that claims founded upon judicial surety bonds and undertakings securing unmatured obligations shall be deemed to be unliquidated and undetermined demands within the meaning of this section.

1043. In any proceeding under this article, the commissioner, as conservator or as liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary mutualize or reinsure the business of such person, or enter into rehabilitation agreements. Such rehabilitation or reinsurance agreements shall provide that, subsequent to the date thereof and for such period of time as the commissioner may determine, no investment or reinvestment of the assets of the person rehabilitated or reinsured shall be made without first obtaining the written approval of the commissioner.